

<b>BULLETIN NUMBER:</b>	<b>PENS-10-003</b>
<b>TITLE:</b>	<b>LETTERS OF CREDIT TO FUND SOLVENCY DEFICIENCIES</b>
<b>LEGISLATION:</b>	<b>PENSION BENEFITS STANDARDS REGULATION</b>
<b>DATE:</b>	<b>AUGUST 2010</b>
<b>DISTRIBUTION:</b>	<b>PENSION PLAN ADMINISTRATORS, FUND HOLDERS, AUDITORS, CONSULTANTS, AND ACTUARIES</b>

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## Overview

The Pension Benefits Standards Regulation (the “Regulation”) permits defined benefit pension plans to fund solvency deficiencies with a letter of credit. Pension plans considering applying to use a letter of credit for solvency deficiency funding should thoroughly review section 35.1 of the Regulation before submitting an application. Both pension plan administrators and fund holders face significant obligations if a letter of credit is utilized to fund a solvency deficiency.

The key regulatory requirements are listed below:

### **A. Procedures at Initiation of a Letter of Credit**

To initiate the use of a letter of credit for funding a solvency deficiency, a pension plan administrator must forward two items to the Superintendent **90 days** prior to the due date of the first solvency deficiency payment to be covered by the letter of credit:

- 1) the executed letter of credit or a certified copy of it, and
- 2) a written statement from the administrator that the letter of credit meets all requirements under section 35.1 (3) (a) to (g); meets certain rules under the international standards for letters of credit; and, meets all related requirements under the Income Tax Act.

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A key requirement is section 35.1 (3) (c), which highlights that a letter of credit must be made out to the benefit of the fund holder in trust for the pension plan.\*

**\*Please note:** a letter of credit is **not** to be made out to the trustees of a pension plan nor to a pension plan's sponsor.

Under sections 35.1 (9) and (10), if the Superintendent finds that a pension plan's proposed letter of credit is non-conforming, she may notify the plan administrator that it is not compliant with the requirements of the Regulation and the pension plan is required to immediately make the solvency payments required by section 35 (3) (c) of the Regulation.

The requirements for the written statement from the administrator are detailed under section 35.1 (4).

### **B. Procedures at Expiration of a Letter of Credit**

A letter of credit must be renewed at least annually until such time as it is replaced with a new letter of credit or a new actuarial valuation report is submitted showing the financial position of the pension has improved and the letter of credit is no longer required. Special conditions apply under section 35.1 (7) if a replacement letter of credit is to be for a smaller amount.

For all three circumstances 1) renewal of an existing letter of credit; 2) replacement of an existing letter of credit; or 3) submission of a new actuarial valuation report showing an improved financial position, the deadline for submitting copies of the applicable document is **90 days** prior to the expiration of the existing letter of credit. Please see section 35.1 (6) (c) for further requirements when a pension plan is seeking to let a letter of credit expire without renewal or replacement.

### **C. Procedures when Plan Funding is Affected by Benefit Enhancements**

Section 6 (4) of the Regulation requires that new funding information be provided for a pension plan whenever benefit improvements are adopted. If the required solvency payments increase as a result of benefit improvements and the plan administrator wishes to fund those payments with a letter of credit, a replacement letter of credit for the larger amount will be required before registration of the related amendments.

## **D. Fund Holder Obligations**

Under section 35.1 (13), a fund holder must demand full payment of a letter of credit if a pension plan has not forwarded documents required under section 35.1 (6), (7), (8) or (11) at least **14 days** prior to the expiry of an existing letter of credit.

A fund holder should review all requirements under section 35.1 (14) through 35.1 (18) relating to plan terminations.

## **E. Fees for a Letter of Credit**

Under section 35.1 (22), the employer is responsible for all fees incurred to establish and maintain a letter of credit. No fees related to the letter of credit may be charged to the pension plan.

## **F. Calculation of Solvency Ratios**

Under section 35.1 (24), a letter of credit is not an asset of a pension plan for purposes of determining its solvency ratio or going concern assets.

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