Manitoba

Office of the Superintendent - Pension Commission

Policy Bulletin #10

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Letters of Credit

Reference: *The Pension Benefits Regulation, amendment 205/2011, Sections 4.18.1*

The *Pension Benefits Regulation* (regulation) was amended effective January 1, 2012 to permit an employer with a defined benefit plan, other than an employer under a multi-unit pension plan, to secure some or all of a plan's solvency special payments through a letter of credit that meets certain prescribed requirements. The letter is provided to the fund holder in lieu of making cash remittances with respect to solvency special payments.

This update has been prepared to outline the legislative requirements and related guidelines under *The Pension Benefits Act* (Act) and the regulation related to the use of letters of credit to fund plan solvency deficiencies.

Definitions

The following definitions apply to letter of credits.

"holder" means the fund holder that is the beneficiary under a letter of credit used to secure special payments, or the fund holder's successor.

"issuer" means the issuer of a letter of credit.

"qualified issuer" means a bank that is a member of the Canadian Payments Association and has one of the following credit ratings:

(a) A or higher, if the rating is given by Dominion Bond Rating Service Limited, Fitch Ratings, or Standard & Poor's Ratings Services; or

(b) A2 or higher, if the rating is given by Moody's Investors Service.

Letter of credit requirements

A letter of credit used to secure special payments must

(a) be an irrevocable and unconditional standby letter of credit;

(b) be issued by a qualified issuer;

(c) comply with the rules of International Standby Practices ISP98 (publication No.590) of the International Chamber of Commerce in effect at the time the letter of credit is issued;

(d) meet, and be issued in accordance with, the requirements of the *Income Tax Act* (Canada);

(e) specify when it takes effect and when it expires;

(f) expire no later than one year from the date it takes effect;

(g) oblige the issuer to make payment on demand by the holder;

(h) be issued in Canadian currency; and

(i) provide that

(i) the beneficiary is the fund holder in trust for the pension fund,

(ii) on demand, the issuer will immediately pay to the holder the amount, not exceeding its face amount, that is demanded, without further inquiry,

(iii) the insolvency or bankruptcy of the employer will not affect the rights and obligations of the issuer or the holder,

(iv) if the issuer decides not to renew the letter of credit on its expiry, the issuer will give written notice to the administrator, the holder and the superintendent of that decision at least 90 days before it expires,

(v) it cannot be assigned, and

(vi) it cannot be amended, except

(A) on renewal, or

(B) if there is a change of holder, to reflect that change.

PROCESS

Letter of credit and statement to be filed

At least 90 days before the first special payment secured by a letter of credit is payable, the administrator must file with the commission a certified copy of the letter of credit and the administrator's written statement confirming that the letter of credit meets the prescribed requirements.

Superintendent to acknowledge receipt
As soon as practicable after receiving a certified copy of a letter of credit, the superintendent must provide written notice to the administrator that the letter of credit has been received.

Administrator to provide letter of credit to holder
The administrator must provide the letter of credit, and a copy of the superintendent's notice of receipt, to the holder

(a) before the first special payment secured by the letter of credit is payable; and

(b) if the letter of credit is to renew or replace another letter of credit, at least 15 days before expiry or cancellation of the other letter of credit.

Letter of credit must be maintained
The employer must maintain a letter of credit in force, and renew or replace it before it expires, without any decrease in the amount secured unless

(a) the employer has paid into the plan all special payments secured by the letter of credit, plus interest as required by the regulation for these payments;

(b) an actuarial valuation report and cost certificate filed with the commission show that the funding requirements of the regulation will continue to be met without the letter of credit;

(c) the employer has paid into the plan the amount that an actuarial valuation report and cost certificate filed with the commission shows to be sufficient to meet the funding requirements of the regulation;

(d) the letter of credit has been renewed or replaced with a letter of credit that secures a reduced amount as permitted under the regulation; or

(e) if the plan is terminating, the superintendent has approved a termination report and the employer has paid any amount required to be paid as special payments on termination.

Amount of renewing or replacing letter of credit
The amount secured by a renewing or replacing letter of credit may be less than the amount secured by the original letter of credit if

(a) the employer has paid into the plan a portion of the amount secured by the original letter of credit and the renewing or replacing letter of credit secures the balance of that amount; or

(b) an actuarial valuation report and cost certificate filed with the commission show that the funding requirements of the regulation can be met by securing or paying a lesser amount, and

(i) the renewing or replacing letter of credit secures that amount, or

(ii) the employer has paid into the plan a portion of that amount and the renewing or replacing letter of credit secures the balance of that amount.

Expiry or cancellation
At least 90 days before a letter of credit expires or is cancelled, the administrator must

(a) advise the superintendent and the holder in writing whether the letter of credit will be renewed, replaced or allowed to expire without renewal or replacement; and

(b) file the documents required to be filed with the commission under the regulation when either a letter of credit expires without renewal or replacement or is to be renewed or replaced.

Filing when letter of credit expiring without renewal or replacement
If the letter of credit will not be renewed or replaced, the administrator must file with the commission

(a) confirmation that all special payments secured by a letter of credit plus interest required by the regulation for these payments has been paid;

(b) the actuarial valuation report and cost certificate showing that the funding requirements of the regulation will continue to be met without the letter of credit; or

(c) the actuarial valuation report, a cost certificate, and confirmation of the payment by the employer of the amount that an actuarial valuation report and cost certificate filed with the commission shows to be sufficient to meet the funding requirements of the regulation.

<u>Filing when letter of credit to be renewed or replaced</u>
If the letter of credit will be renewed or replaced, the administrator must file with the commission

(a) a certified copy of the renewing or replacing letter of credit and the administrator's written statement that the renewing or replacing letter of credit meets the prescribed requirements; and

(b) if the amount secured by the renewing or replacing letter of credit will be less than the amount secured by the original letter of credit,

(i) confirmation of the payment of, the portion of the amount secured by the original letter of credit and that the renewing or replacing letter of credit secures the balance of that amount, or

(ii) the actuarial valuation report and cost certificate showing that the funding requirements of the regulation can be met by securing or paying a lesser amount and, if applicable, confirmation that the employer has paid into the plan a portion of the amount and the renewing or replacing letter of credit secures the balance of that amount.

<u>Plan termination</u>
If a plan or a part of a plan is to be terminated, the employer must maintain a letter of credit used to secure special payments in force, and, before it expires, renew or replace it without any decrease in the amount covered, until

(a) the superintendent has approved a termination report; and

(b) the employer or issuer has paid the special payments required to be paid termination.

Within 14 days after the superintendent's approval of a termination report, the employer must pay into the plan

(a) all special payments secured by a letter of credit, plus interest as required by the regulation for these payments; less

(b) the surplus, if any.

When notifying the administrator that the termination report is approved, the superintendent must notify the administrator and the holder of any amount payable as special payments on termination under the regulation and the date by which it is payable.

If the employer fails to pay the full amount required to be paid as a special payment on termination under the regulation on or before the day it is due, the holder must, on the next business day, demand that the issuer pay under the letter of credit the amount payable as the special payment on termination under the regulation.

If the plan has a solvency deficiency after payment of the amount payable as special payment on termination under the regulation, the remaining solvency deficiency must be amortized over a period of not more than 5 years from the review date which is the date of termination.

<u>Holder to demand payment under letter of credit</u>
The holder must demand payment under a letter of credit 14 days before the letter of credit expires, unless the holder has received

(a) copies of documents required to filed under the regulation when a letter of credit is expiring without renewal or replacement;

(b) a renewing or replacing letter of credit and copies of the documents required to be filed under the regulation when a letter of credit is to be renewed or replaced; or

(c) if the plan is to be terminated, the superintendent's approval of the termination report and the special payments on termination required to be made under the regulation, if any.

A demand for payment under a letter of credit must be made in the form required or permitted in the letter of credit.

<u>Interest</u>
Interest is payable on each special payment secured by a letter of credit from the date the special payment is due at the interest rate used to establish the solvency deficiency. The employer must pay the interest monthly no later than 30 days after the end of the month for which the interest is payable, unless the interest payable under this subsection is secured by the letter of credit.

<u>Employer to pay costs</u>
The employer must pay the costs of obtaining and maintaining a letter of credit and those costs must not be charged to the plan.

<u>Transfer deficiencies</u>
If funds are secured by a letter of credit, before making a transfer that would result in a transfer deficiency under the regulation, the employer must pay into the plan the lesser of

(a) the total of all special payments secured by a letter of credit, plus interest as required by the regulation for these payments; or

(b) an amount sufficient to eliminate the transfer deficiency.

<u>Impact on actuarial valuations</u>
Funds secured by a letter of credit are not assets of the plan and may not therefore be used for purposes of determining the going concern assets or solvency ratio of the plan.

Amounts secured by a letter of credit whose effective date is prior to the valuation date may however be included as a solvency asset for purpose of determining the solvency deficiency of the plan.

<u>Timelines for Remittance Apply</u>
Letters of credit are considered remittance under the Act and must be provided to the fund holder within the times required under subsection 4.18(2).

If you have any questions regarding this bulletin you may contact us at:

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**** Available in English Only ****

This bulletin has no legal authority. The Pension Benefits Act of Manitoba and the Pension Benefits Regulation should be used to determine specific requirements.