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Multi-employer pension plans and IFRS standards: Who holds the risk?

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When Canada moves to the international accounting standards (IFRS) the rules for multi-employer pension plans (MEPPs) will change.

There are about 1.5 million Canadians who belong to multi-employer pension plans, either in the public sector or in the private sector. This compares to 3 million in all other employer-sponsored pension plans.

Under international accounting standards a multi-employer plan is any plan where a company shares actuarial risks with other companies. These actuarial risks are those associated with all current and former employees of all the companies, and are not limited to a single company's current and former employees. Basically, benefits and contribution levels are not set at the company level, but are set at a plan level.

Under IFRS rules, employers who contribute to a MEPP on behalf of their employees may have to change how they account for their MEPP. Many employers currently account for their MEPP as a defined contribution plan. The employers hold no liability on their balance sheet, and only expense actual contributions in the income statement. Under the international standard for post-retirement employee benefits (IAS19) multi-employer plans are to be valued the same as a single-employer defined benefit plan, except the liabilities and expense are first determined at the plan level and then allocated to the various participating companies.

IFRS recognizes that some companies may not have access to the plan information to complete a valuation on a defined benefit plan basis, or that the allocation of the plan liabilities and expenses to the various participating employers may not be consistent or reliable. For these employers the international standard allows the use of defined contribution accounting—for now.

The international standard-setting body did attempt to re-define multi-employer plans and to increase the number of employers that would have to value their multi-employer plan liabilities and expense on a defined benefit basis. After criticism of their proposal by the international community, the proposal was removed from consideration. But employers need to be aware of what could be in store for them.

Who holds the risk?

The key premise of the international standard is that companies should recognize a multi-employer plan as a defined benefit plan if the plan's deficit or surplus can affect the company's future contributions. In simple terms, the question is decided by determining who holds the risks.

Under Quebec law a multi-employer plan cannot decrease benefits for its Quebec members. While MEPPs are still trying to cope with this restriction, this could mean the trustees of a MEPP may attempt to hold the Quebec employer responsible for any deficit. It would seem that under international standards these employers must make the effort to value their multi-employer plans under the defined benefit rules. Small employers may be able to argue that they cannot obtain the essential information to perform this valuation. However, larger employers may have difficulty convincing their auditors that they do not have or could not get access to the information.

In Ontario, multi-employer plans can be structured so that employers are not responsible for any future deficits. In these plans it is the members and former

members who bear all the actuarial risks. Deficits are handled by decreasing benefits or by negotiating additional contributions during the next round of collective bargaining. These employers could still use the defined contribution standard and their pension expense would be their actual contribution to the plan. Since they are not responsible for funding any deficits there is no liability (or asset) to hold on their balance sheet.

However, some Ontario plans do require employers to fund deficits. Under the international standards, these employers will have to adopt defined benefit accounting. They could continue to use the old method only if they can convince their auditors that they cannot accurately measure their risk to future contributions using the defined benefit accounting method.

How can employers and administrators of multi-employer plans prepare for international accounting standards?

First, they need to review their plan documents, trust agreements, collective bargaining agreements and employee communications to determine the substantive plan. It is always best that all these sources agree, however the accountants give a great deal of credence to what has been promised and what has been done in the past. Even if the actual plan documentation is less generous than what has been promised or actually done in the past, the accountants will require the more generous plan or the “substantive plan” to be valued.

(The most famous example of Ontario MEPP employers receiving a pension shock is the case involving the Participating Co-Ops MEPP. When the plan was wound up the employers were surprised to find that the Trustees could not decrease benefits, and as a result the regulator expected the employers to fund the deficit. This was the result of the wording in the plan text.)

Second, the employers need to decide if their future contributions will be influenced by the plan’s deficit. If the employer has Quebec members then the answer is likely “yes”. If the plan is such that all the risks are assumed by the plan members then the employer can rely on defined contribution accounting. But if any part of the risks remains with the employer then defined benefit accounting must be considered.

Third, the employers need to decide if accounting for their multi-employer plan on a defined benefit basis is even possible. It is here that employers are at risk that the international accounting standard will be revised to narrow the number of exceptions. What may seem impossible today may become possible tomorrow.

Canada is slowly adopting international standards and the U.S. intends to converge its standards with the International Standards. Now is the time for employers to review their multi-employer plan, to consider how defined benefit accounting could be applied to their plans, and to be prepared for any accounting changes.

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