

Consultation Paper on issuance of GUIDELINES FOR THE 'CONVERSION' OR 'SHIFT' OF DEFINED BENEFIT PENSION SCHEMES TO DEFINED CONTRIBUTION PENSION SCHEMES

PART A - Preliminary

1.0 Purpose of the Consultation Paper

- 1.1. This Consultation Paper (“CP”) sets out the proposed approach to be taken by the Financial Services Commission (“the Commission”) in relation to the conversion or shift of Defined Benefit Pension Schemes to Defined Contribution Pension Schemes in Mauritius.
- 1.2. Based on the approach proposed in this CP and the feedback received during the consultation period, the Commission shall finalise the Guidelines for the conversion or shift of Defined Benefit Pension Schemes to Defined Contribution Pension Schemes. These Guidelines shall be issued by the Commission pursuant to its powers under section 7(1) (a) of the Financial Services Act 2007 (the “FSA”).
- 1.3. This CP is not intended to, does not, and may not be relied upon to create any rights, substantive or procedural, enforceable at law by any party in any matter, civil or criminal.

1.4. The consultative period will run from 27 February 2020 to 27 March 2020. Your views and comments should be submitted at the following email address: pensionsconsultation@fscmauriti.us.org

2.0 Definitions

“actuarial assumptions” means assumptions as prescribed under Appendix 2;

“ancillary benefit” means any benefit ancillary to the pension benefit and shall include disability benefits, death benefits , pre-retirement death benefits and early retirement benefits;

“conversion” means the process of converting a defined benefit scheme to a defined contribution scheme by commuting the members’ benefits that have accrued up to the date of conversion and crediting the commuted value to the members’ accounts under the subsequent defined contribution scheme;

“shift” means the process of shifting the members of a defined benefit scheme to a defined contribution scheme, for future service accrual, on the date on which the accrued pension benefits of members under the defined benefit scheme are preserved with link to future salary or salary drawn by the member on the shift date, as may be applicable;

“solvency basis” means the calculation of accrued liabilities of the scheme assuming that the scheme is discontinued on the valuation date in accordance with the actuarial assumptions in Part I of Appendix 2;

“solvency ratio” means the ratio of fair value of assets to the solvency liabilities as determined by the actuary of the scheme in accordance with the actuarial assumptions in Part I of Appendix 2;

“valuation date” means the conversion date or the shift date.

3.0 Background

The conversion or shift of a defined benefit scheme to a defined contribution scheme alters the fundamental pension agreement between the employer and the scheme members.

It is recognized that sponsoring employers are entitled to change the basic structure of a pension scheme for future benefits.

While each case presents its own circumstances, the following guidelines are set out to assist such conversions or shifts.

Prior to applying for conversion or shift, the applicant shall ensure compliance with section 8 of the Private Pension Schemes Act.

4.0 Application process

4.1 The application for the approval of a conversion or a shift of a defined benefit scheme to a defined contribution scheme shall be accompanied by the following documents –

- (a) A conversion plan or shift plan, certified by all members of the governing body of the scheme, and that shall include the rationale for conversion

or shift, as the case may be and the way forward in treating any deferred members and pensioner;

- (b) An actuarial valuation report as at conversion date or shift date;
- (c) A notice of amendment to the constitutive documents of the scheme given to all affected scheme members;
- (d) Amended constitutive documents of the scheme for the Commission's approval together with duly approved resolutions signed respectively by all members of the governing body of the scheme and the board members of the sponsoring employer;
- (e) A funding plan, where applicable, to restore solvency ratio to 100%;
- (f) Evidence of the communication exercise to members of the scheme;
- (g) Certified true copies of signed option forms evidencing consents of members of the scheme to convert or shift; and
- (h) Such other documents or information as may be required by the Commission.

4.2 The Commission shall on a case to case basis, assess each application and in its assessment, the Commission shall have regard to the interests of concerned scheme members as well as the sustainability of the scheme.

PART B - Conversion: Defined Benefit to Defined Contribution Scheme

5.0 Application of this part

This part applies to scheme conversions where the scheme is changed from a defined benefit scheme to a defined contribution scheme, the members' benefits that have accrued up to the date of conversion are commuted and the

commuted value is credited toward the members' accounts under the subsequent defined contribution scheme.

5.1 Conversion of fully funded DB schemes

Where a defined benefit scheme is fully funded at the conversion date, a conversion to a defined contribution scheme shall be permitted provided the following conditions are satisfied –

- (a) Full disclosure of information to members;
- (b) Consent of all members is obtained;
- (c) Communication to members of all the options available to them; and
- (d) The constitutive documents of the scheme allow for the conversion.

Evidence of the fulfillment of the above conditions shall be communicated to the Commission within 14 days of the communication exercise.

5.1.1 Full disclosure of information to members

Prior to the conversion, the scheme shall give a written statement of benefits and options to the members being affected by the conversion within 7 days of the communication exercise once the members' entitlements and commuted values have been determined. The statement of benefits shall contain, at a minimum, the information specified in Appendix 1.

5.1.1.1 Minimum Commuted Value

The commuted value of the accrued benefits as of the date of conversion must be determined for each consenting member.

The commuted value of a pension, deferred pension or ancillary benefit shall be calculated on a conversion basis using methods and actuarial assumptions as specified in Part II of Appendix 2.

The value of ancillary benefits for which the member has met all eligibility requirements under the pension plan as of the date of conversion, must be taken into account in determining the commuted value of the member's accrued benefits.

However, sponsoring employers may wish to contribute above the minimum commuted value so as to better compensate the members for the loss in their guaranteed benefits under the defined benefit scheme.

5.1.1.2 Salary Projections

Where a scheme is structured such that benefits are related to final earnings of a member, a projection of salary increases must be taken into account in calculating the commuted value of the accrued benefits unless the constitutive documents of the scheme clearly provides that salary projection need not be taken into account on a scheme conversion.

If the constitutive documents of the scheme are amended to freeze the salary level at which the accrued benefits are determined as of the date of conversion, notice of this amendment to freeze the salary level must be included as part of the notice of amendment given to all affected scheme members.

5.1.2 Consent of members

Where a member is affected by the conversion, the sponsoring employer shall give the member the opportunity to give his or her consent within such reasonable time as the sponsoring employer may determine.

Proof of all consents obtained shall be submitted to the Commission.

5.1.3 Options to Members

All members of the defined benefit scheme to whom the conversion applies shall be given the option of preserving their accrued benefits in the form of a defined benefit. The member may either elect to convert his or her accrued pension benefits to a defined contribution form or may elect to stay in the defined benefit scheme for future accrual of benefits.

(a) Elect to convert

Where a member has elected to convert his or her accrued pension benefits to a defined contribution form, the sponsoring employer shall inform the member of the amount of pension benefits he or she is foregoing under the defined benefit plan.

In the event that all members of the defined benefit scheme have elected to convert their accrued pension benefits to a defined contribution form, the defined benefit scheme shall eventually no longer exist and the private pension scheme licence shall be held by the defined contribution scheme unless there is a change in the name of the scheme.

(b) Elect not to convert

Where a member has elected not to convert his or her accrued pension benefits to a defined contribution form, the member shall be allowed to remain in the defined benefit scheme without any change, whatsoever, to his or her accrued and future benefits.

(c) No election made

If no election is made, the member is considered not to have elected to convert his or her accrued pension benefits to a defined contribution form.

5.1.4 Amendment to the constitutive documents of the scheme

Scheme conversions shall only be effected by means of an amendment to the constitutive documents of the scheme for which the approval of the Commission shall be obtained in accordance with section 29 of the Private Pension Schemes Act. In processing the application for approval, the Commission shall have regard to:

- (a) the funding level of the scheme;
- (b) compliance with the Act, Regulations and Rules made under the Act;
- (c) compliance with these guidelines; and
- (d) the outcome of the communication exercise conducted by the sponsoring employer to the members of the scheme.

5.2 Conversion of under-funded defined benefit schemes

The requirements in Part 5.1 shall apply *mutadis mutandis* to the conversion of under-funded defined benefit schemes. If the assets of the scheme are not sufficient to cover the commuted value of the benefits that are to be converted and the annuities purchased pursuant to the conversion, the sponsoring employer shall contribute the shortfall to the scheme in a lump sum.

The sponsoring employer shall make a lump sum payment to the DB scheme to ensure that the solvency ratio is not less than 1.0.

PART C - Shift: Shift members from Defined Benefit to Defined Contribution

6.0 Application of this part of the guidelines

This part applies to cases where the members of a defined benefit scheme shift to a defined contribution scheme, for future service accrual, on the date on which accrual to the defined benefit scheme stops (“the shift date”).

6.1 Shift of fully funded defined benefit schemes

Where a defined benefit scheme is fully funded at the shift date, the shift to a defined contribution scheme shall be permitted provided the following conditions are satisfied –

- (a) Full disclosure of information to members;
- (b) Consent of all contributing members is obtained;
- (c) Communication to members of all the options available to them;
and
- (d) The constitutive documents of the scheme allow for the shift.

Evidence of the fulfillment of the above conditions shall be communicated to the Commission within 14 days of the communication exercise.

6.1.1 Full disclosure of information to members

Prior to the shift, the scheme shall give a written statement of benefits and options to the members being affected by the shift within 7 days of the communication exercise. The statement of benefits shall contain, at a minimum, the information specified in Appendix 1.

6.1.2 Consent of members

Where a member is affected by the shift, the sponsoring employer shall give the member the opportunity to give his or her consent within such reasonable time as the sponsoring employer may determine.

Proof of all consents obtained shall be submitted to the Commission.

6.1.3 Options to Members

All members of the defined benefit scheme to whom the shift applies shall be given the option of remaining in the defined benefit scheme. The member may either elect to shift to a defined contribution scheme or may elect to stay in the defined benefit scheme.

(a) Elect to shift

Where a member has elected to shift to a defined contribution scheme, the member shall be allowed to preserve his or her past service benefits with a link to future final salary at the appropriate retirement age under the defined benefit scheme.

In the event that all members of the defined benefit scheme have elected to shift to a defined contribution scheme, the defined benefit scheme shall be frozen with link to future final salary at appropriate retirement age. In exceptional cases, the defined benefit scheme may be frozen with link to the salary drawn by the member on the shift date where the sponsoring employer has provided proof of non-affordability to the Commission by way of financial statements and an independent assessment by an audit firm.

If the sponsoring employer elects to purchase an annuity for the members with regard to their accrued benefits in the defined benefit form, the annuity shall comply with all the requirements of the constitutive documents of the scheme and the Act including provisions on early retirement, transfer rights and pre-retirement death benefits.

(b) Elect not to shift

Where a member has elected not to shift to a defined contribution scheme, the member shall be allowed to remain in the defined benefit scheme without any change, whatsoever, to his or her accrued and future benefits.

(c) No election made

If no election is made, the member is considered not to have elected to shift to the defined contribution scheme and shall remain in the defined benefit scheme without any change, whatsoever, to his or her accrued and future benefits.

6.1.4 Amendment to the constitutive documents of the scheme

Scheme shifts shall only be effected by means of an amendment to the constitutive documents of the scheme for which the approval of the Commission shall be obtained in accordance with section 29 of the Private Pension Schemes Act 2012. In processing the application for approval, the Commission shall have regard to:

- (a) the funding level of the scheme;
- (b) compliance with the Act, Regulations and Rules made under the Act;
- (c) compliance with these guidelines; and
- (d) the outcome of the communication exercise conducted by the sponsoring employer to the members of the scheme.

If the constitutive documents of the scheme are amended to freeze the salary level at which the accrued benefits are determined as at the shift date, notice of this amendment to freeze the salary level must be included as part of the notice of amendment given to all affected scheme members.

6.2 Shift of under-funded defined benefit schemes

The requirements provided in Part 6.1 shall apply *mutadis mutandis* to the shift of under-funded defined benefit schemes. In addition, prior to giving its approval for the shift, the Commission shall also require that the under-funded defined benefit schemes be funded at 100% on a solvency basis or that a contingency plan be submitted to the Commission for approval.

6.2.1 Funding

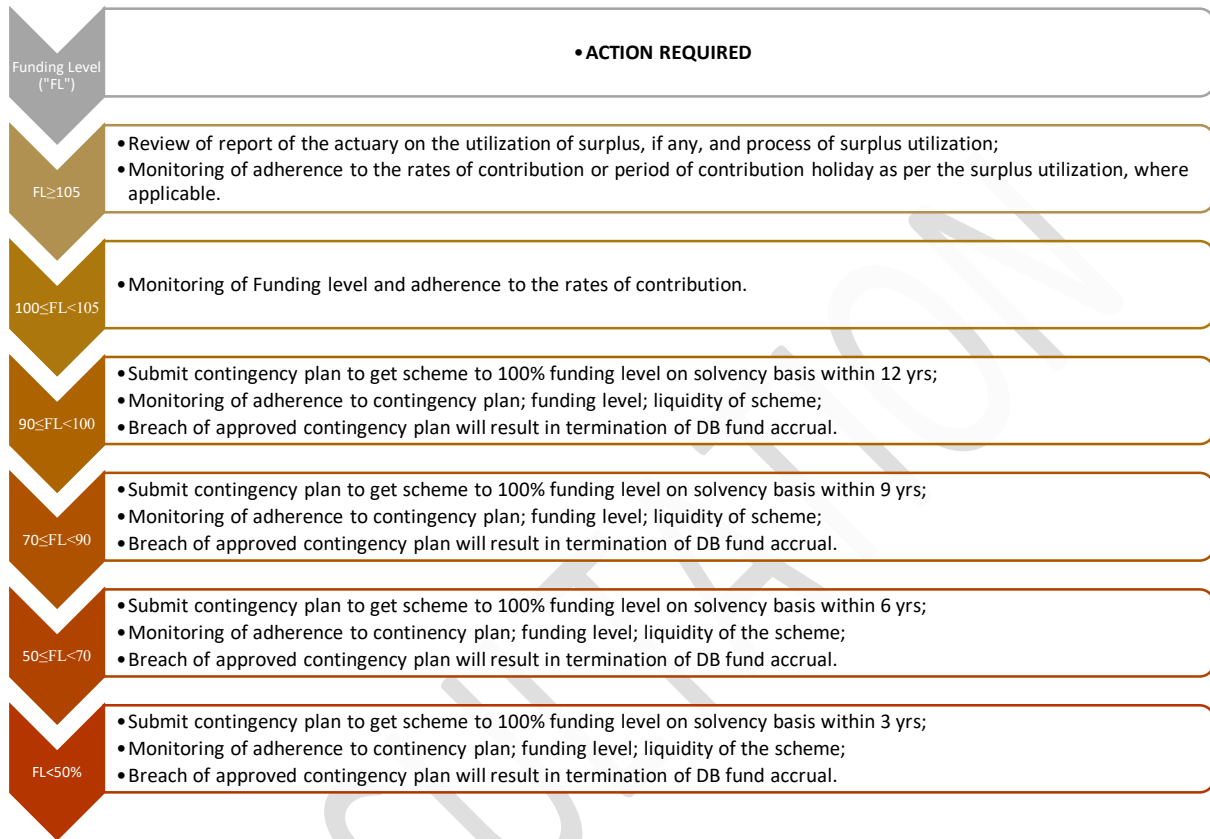
Where the funding ratio of a defined benefit scheme is below 100%, the sponsoring employer shall contribute the shortfall on solvency basis to the scheme in a lump sum.

The sponsoring employer shall make a lump sum payment to the DB scheme to ensure that the solvency ratio is not less than 1.0.

6.2.2 Contingency plan

Where the sponsoring employer is unable to fund the deficit forthwith, the sponsoring employer shall submit a contingency plan to the Commission for approval. Prior to granting its approval, the Commission shall have regard to the amount of deficit of the defined benefit scheme and the proposed time period for funding.

In determining the contents of the contingency plan, the licensee shall have regard to the following –



Issued by the Financial Services Commission for consultation

Date: 27 February 2020

Appendix 1

STATEMENT OF BENEFITS AND OPTIONS FOR MEMBERS

Part I - CONVERSION

The following information must be included in the Statement of Benefits and Options given to each member upon determination of the member's entitlements and commuted values from the defined benefit scheme –

1. A statement that the member may elect not to convert the accrued pension benefits and instead retain all entitlements under the existing defined benefit scheme.
2. If the member elects to convert the accrued pension benefits of a defined benefit scheme, the amount of accrued pension benefits and therefore, the commuted value that shall be credited to the member's defined contribution account shall include the amount and value of:
 - a. ancillary benefits for which the member has satisfied all eligibility requirements; and
 - b. any benefit improvement granted in conjunction with the conversion.
3. The amount, in Mauritian Rupees, of pension benefits at appropriate retirement age that the member is foregoing under the defined benefit scheme.
4. A statement that the member will no longer be entitled to the benefits under the defined benefit scheme, and that the member's future pension

benefits will depend on the earnings of the defined contribution scheme and where applicable, the annuity rates in effect at the time the member is retiring and chooses to annuitize the benefit, except with respect to benefits not converted.

- 5. Identification of any ancillary benefit for which the member has not met the eligibility requirements, and that these ancillary benefits, as the case maybe, will no longer be offered in the defined contribution scheme.**
- 6. A statement that the defined contribution members' account is subject to the constitutive documents of the defined contribution scheme.**

CONSULTATION

Part II - SHIFT

The following information must be included in the Statement of Benefits and Options given to each member upon determination of the member's entitlements from the defined benefit scheme –

1. A statement that the member may elect not to shift to the defined contribution scheme and instead retain all entitlements under the existing defined benefit scheme.
2. If the member elects to shift to a defined contribution scheme, the amount, in Mauritian Rupees, of his or her past service benefits, calculated as at shift date, with a link to future final salary at the appropriate retirement age under the defined benefit scheme.
3. A statement that the member will no longer accrue pension benefits under the defined benefit scheme as at shift date and that the member's future pension benefits will depend on the earnings of the defined contribution scheme and where applicable, the annuity rates in effect at the time the member is retiring and chooses to annuitize the benefit.
4. Identification of any ancillary benefit for which the member has not met the eligibility requirements, and that these ancillary benefits, as the case may be, will no longer be offered in the defined contribution scheme.
5. A statement that the defined contribution members' account is subject to the constitutive documents of the defined contribution scheme.

Appendix 2
ACTUARIAL ASSUMPTIONS
Part I – Solvency Basis

1. **Discount rate:** based on the yield of 20-year Government Bond plus 100 basis point;
2. **Expected salary increases, equal to the expected future inflation plus inflation risk premium**
(Expected future inflation is equal to the difference in yield between 10-year Government Bond and 10-year index-linked Bond
Inflation risk premium is determined based on past 10-year salary increase and CPI data)
3. **Pension increases, as prescribed in the constitutive documents of the scheme, or otherwise as determined by the actuary;**
4. **Mortality rate:** UK or South African mortality tables adjusted for local mortality experience as determined by the actuary, in the absence of Mauritian mortality tables
5. **Lump sum commutation factor:** a cost-neutral factor to be determined by the actuary, unless already prescribed in the constitutive documents of the scheme
6. **Normal Retirement Age, as per Workers’ Rights Act, unless prescribed in the constitutive documents of the scheme**
7. **Any other actuarial assumptions to be agreed upon by the Commission**

Part II – Conversion Basis

- 1. Discount rate: based on the yield of 20-year Government Bond (or any other suitable proxy for risk free rate of return as may be approved by the Commission);**
- 2. Pension increases, as prescribed in the constitutive documents of the scheme, or otherwise as determined by the actuary;**
- 3. Mortality rate: UK or South African mortality tables adjusted for local mortality experience as determined by the actuary, in the absence of Mauritian mortality tables**
- 4. Commutation factor: a cost-neutral factor to be determined by the actuary, unless already prescribed in the constitutive documents of the scheme**
- 5. Normal Retirement Age, as per Workers’ Rights Act, unless prescribed in the constitutive documents of the scheme**
- 6. Any other actuarial assumptions to be agreed upon by the Commission**