What you should know about the Ontario UPP

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FAUW Presentation

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First – some disclaimers

- I do not represent anyone but myself…
- Nothing I say should be construed as financial advice.
- For clarity I have omitted many details for examples in terms and conditions of pension payments.

“Why change to a JSPP”

Information from the UPP web pages

http://www.universitypension.ca/

Joint plan governance by employers and employees, which will give pension plan members a greater voice in governance than in the past

True

More stable and predictable contributions from employers and plan members.

False

Clear and explicit sharing of risk between employers and plan members

Well…

Relief from some of the financial pressures on universities caused by Ontario’s current pension funding rules

False -ish

Pension benefits earned under existing university pension plans will be preserved.

True

Efficiencies and economies of scale
… access to higher-return investment opportunities …
will help address increasing costs

False

Defined Benefit (DB), Defined Contribution (DC), and Hybrids

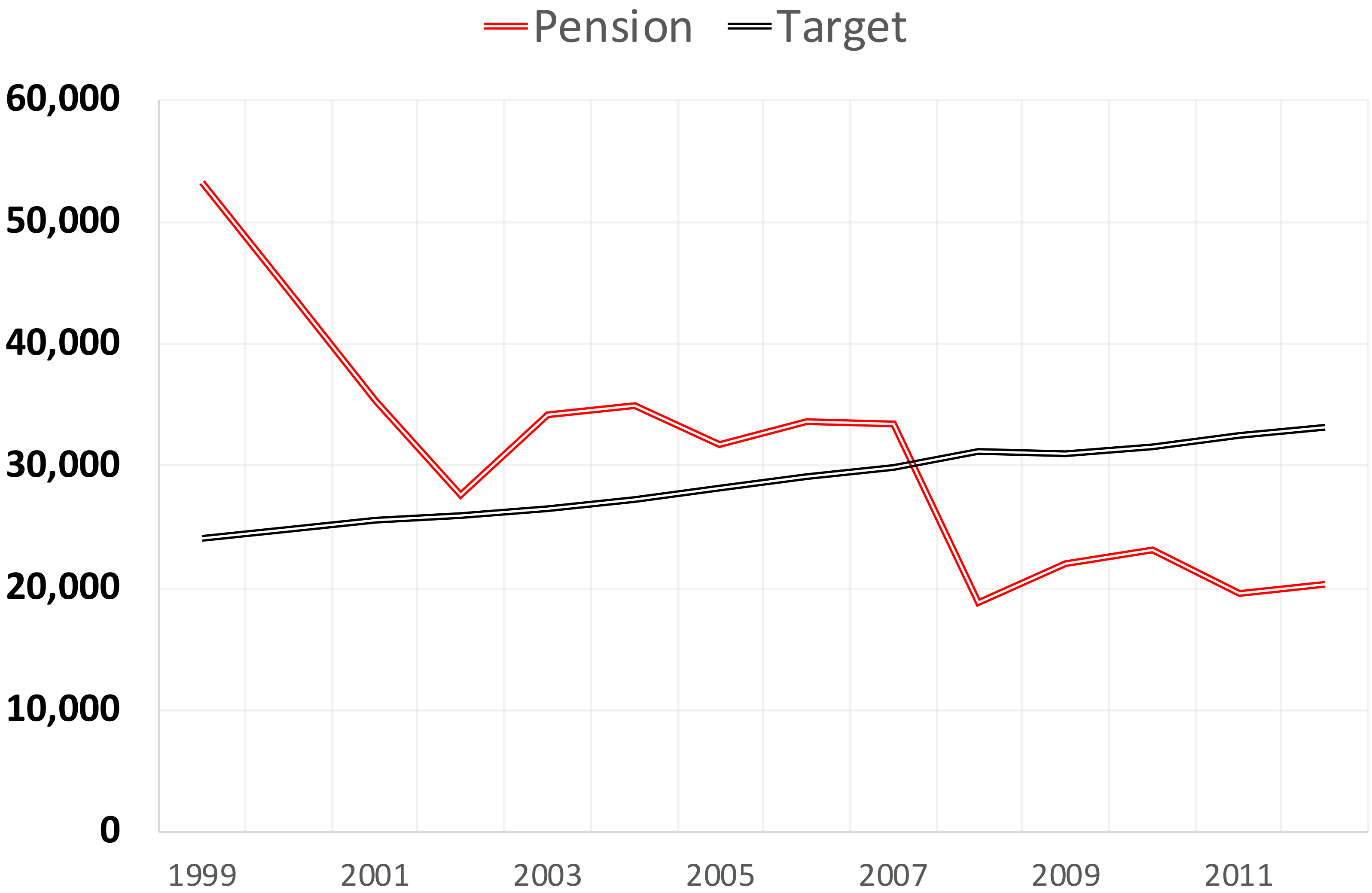
Defined Benefit (DB)

- **DB** plans offer a formula-based pension.
- The cost is uncertain, the benefit is fixed relative to final salary.
- Each year of service adds to the final pension.
  - Major decline in popularity since late 1990s.
  - De-risking, closure, wind-up of existing plans
  - A world-wide phenomenon (USS, UK)
  - Now quite rare for private sector employers
  - Benefit security is a key uncertainty

Defined Contribution

- **Defined Contribution** plans offer an individual fund for each employee
- Contributions are invested and the accumulated proceeds are used to fund retirement income.
- The cost is fixed (relative to salary) the annual pension generated is uncertain.
- Potential for inadequate retirement income and/or dissipation risk.
- Also, potential for windfalls!

ILLUSTRATIVE DC BENEFITS



The University Pension Plan (UPP)

- The UPP is a new **Defined Benefit** pension plan for Ontario Universities.
- It is a **Multi-Employer Pension Plan.**
  - All current Ontario university pension plans are **Single Employer Pension Plans.**
- It is a **Jointly Sponsored Pension Plan.**
  - a 50:50 collaboration between employers and employees.
  - with shared risk, shared contributions and shared governance.

The University Pension Plan Ontario

- Universities may apply to join the UPP.
  - Employees must consent; retirees must be consulted;
  - Universities must contribute sufficient assets to fund the benefits already earned by employees and retirees.

- Currently, **Queen's**, **UT** and **Guelph** are working through the consent process.

The UW Defined Benefit (DB) Plan

- The annual pension calculation is based on the **Final Average Earnings**
- For each year of service in the plan, members will get an annual pension of roughly:
  - 1.4% of FAE up to the "**YMPE**" ($55,900, currently), plus
  - 2% of FAE between the "YMPE" and a maximum pensionable salary (around $190,000)

Feature	UPP	UW
Salary Basis	48 months	60 months
Accrual Rates	1.6%	1.4%
	2.0%	2.0%
Partner’s pension	50%	None*
Early Retirement	60	62
Inflation Protection	75% of CPI Conditional	75% of CPI
Member Contributions	~10.2%*	~7.4%
Pension above IT maximum	No	Yes

The WLU Hybrid (DB Underpin) plan

- WLU has a Defined Contribution (DC) plan with a guaranteed minimum benefit.
  - Contributions are invested for each employee.
  - At retirement, they can take their funds and convert them to an annual pension.
  - If the pension is smaller than the guaranteed minimum, WLU will fund the difference.
  - The guaranteed minimum pension is similar to UW's DB pension.

Feature	UPP	WLU
Salary Basis	48 months	60 months
Accrual Rates	1.6%	1.37%
	2.0%	2.0%
Partner’s pension	50%	None*
Early Retirement	60	None*
Inflation Protection	75% of CPI Conditional	50% of CPI
Member contributions	~10.2%	~8.7%
Type	DB	Hybrid

Question 1

Why are so many Defined Benefit and Hybrid pension plans in trouble?

Years of low interest rates and volatile investment markets have led to funding shortfalls and climbing contribution rates for most university pension plans in Ontario. Together with rising life expectancy, the resulting higher plan costs make it increasingly difficult to meet pension funding needs.

From the UPP Website
http://www.universitypension.ca/WhyJSPP

Question 2

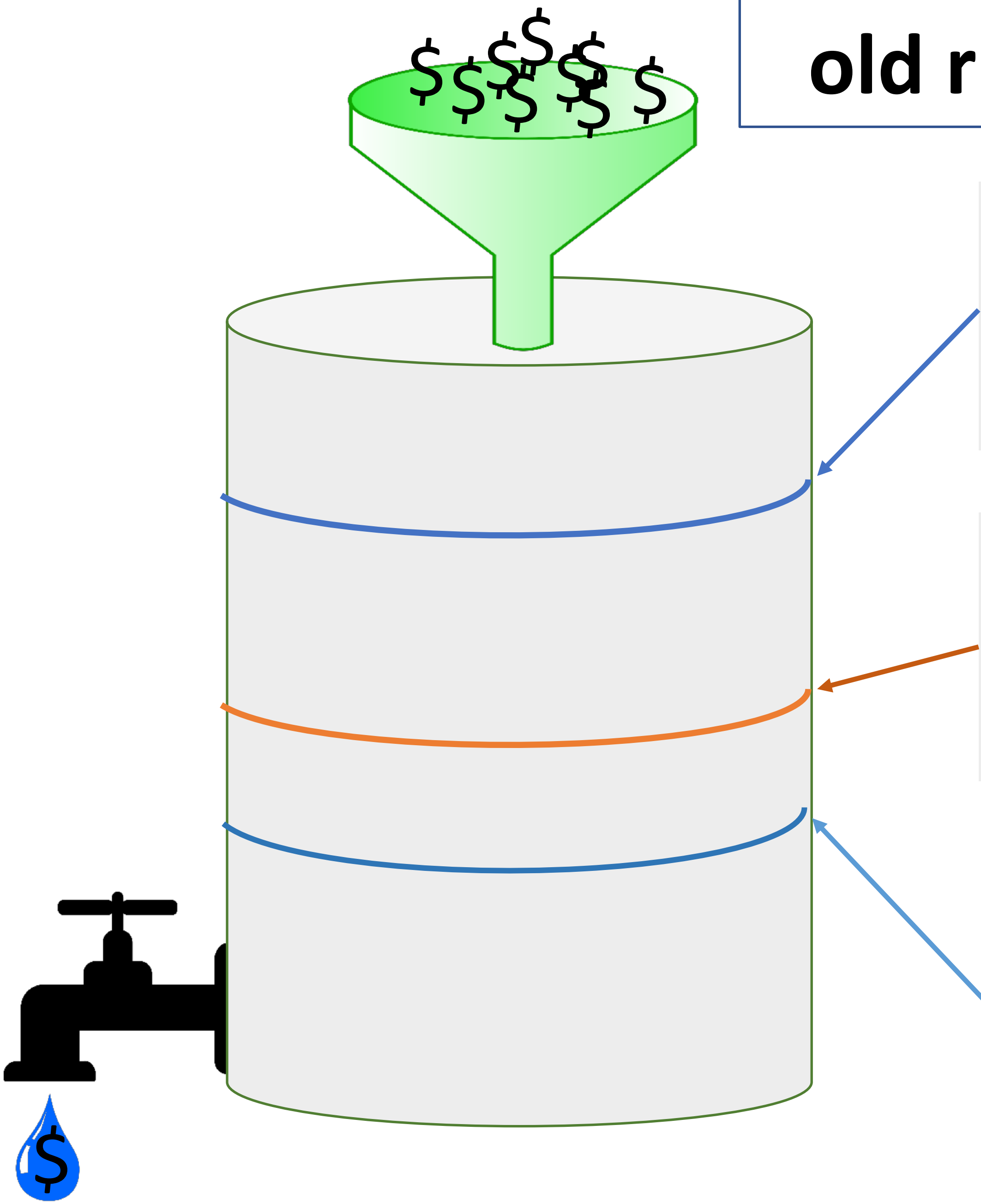
Is the UPP good for employers?

Is the UPP good for employers?

- ✓ Their deficit payments are reduced by moving from a Single Employer pension Plan to a Multi-Employer Pension Plan.
- ✓ They can take longer to pay off the deficits.
- ✓ Ongoing costs are reduced through risk sharing.

It is likely that more universities will want to join the UPP in the next phase.

Funding the Pensions – old rules (up to 2018)

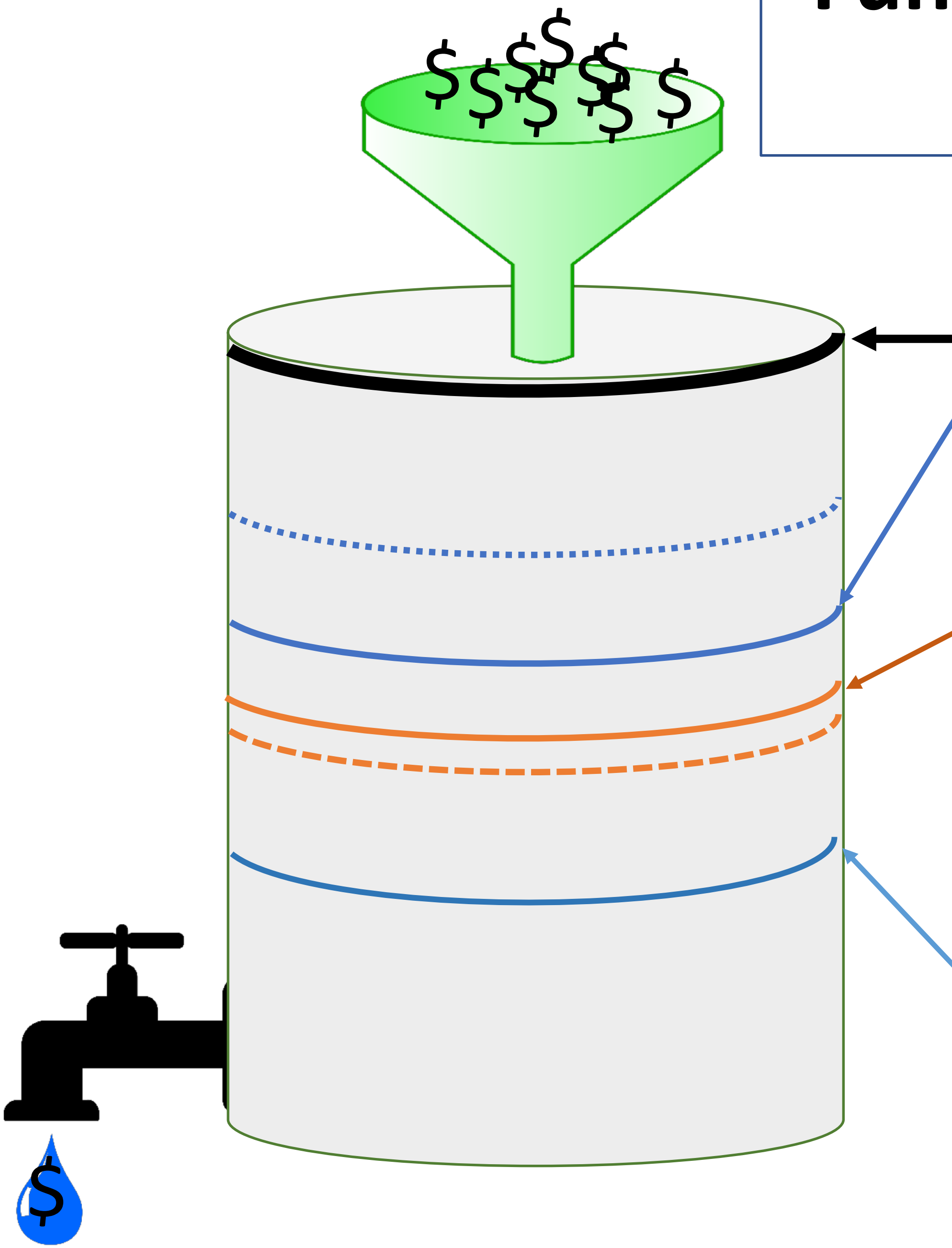


How much money the UX plan needs as a single employer plan

How much money the UX plan needs to give UPP

How much money UX has

Funding the Pensions - New rules

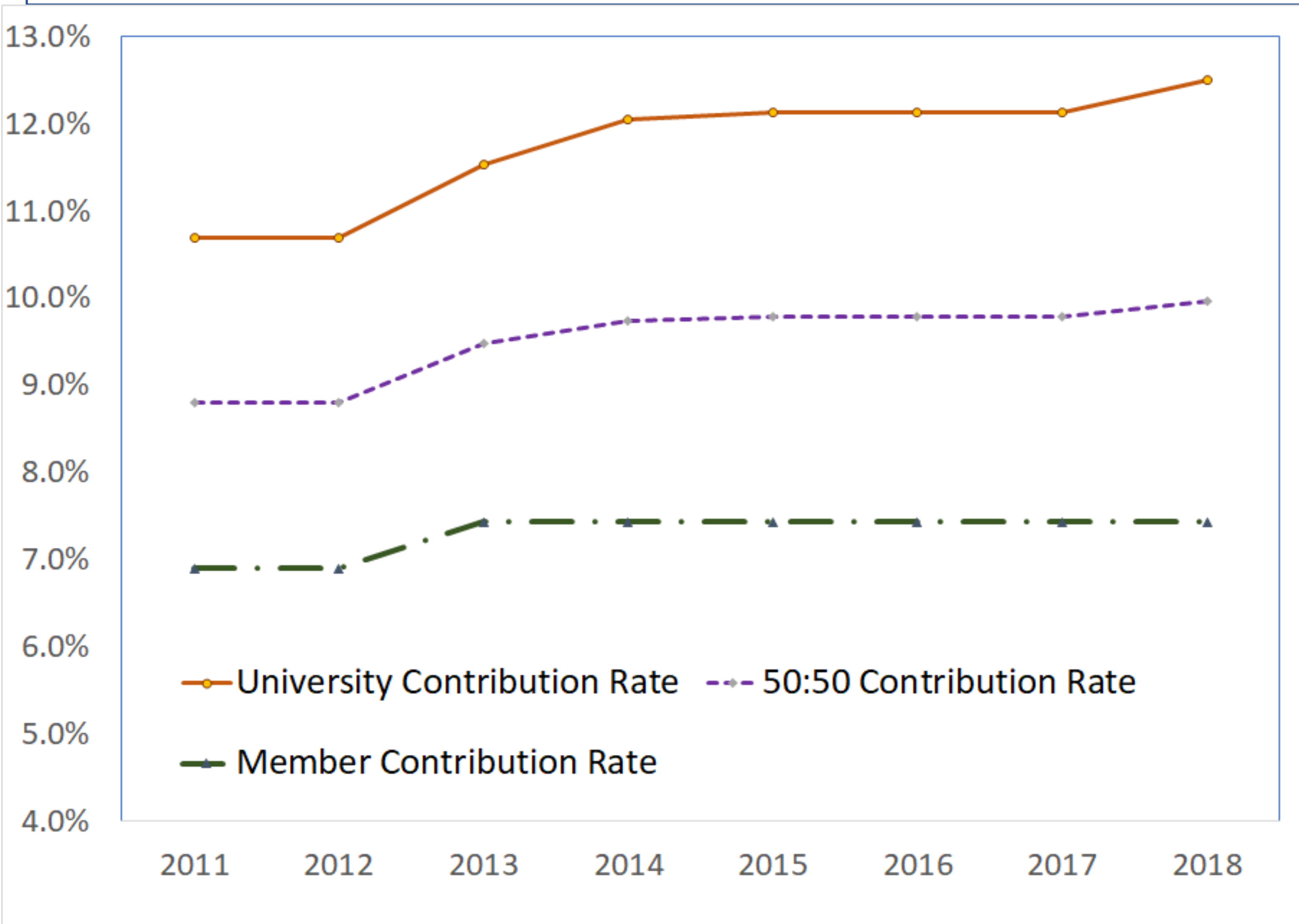


How much money the plan needs to <u>guarantee</u> the benefits

How much money the plan needs as a MEPP

How much money the plan has

UW Contribution rates 2011-2018
% of pay, average salary



Question 3

What's <u>not</u> good about the UPP for employees?

What's <u>not</u> good about the UPP for employees?

- **<u>Benefit Security</u>**
  - Existing plans cannot wind up unless fully funded or the sponsor is bankrupt.
  - **The UPP can wind up at any time and reduce the benefits previously earned in the plan.**
  - Pessimistic scenario:
    - Market crash; major deficit; contributions jump up; plan closed; benefits reduced by ~30%

What's <u>not</u> good about the UPP for employees?

- **<u>Contribution volatility</u>**
  - When investments do poorly, or interest rates fall, the pension plan will need more money.
  - Because UPP is Jointly Sponsored, employees will pay half of the cost, whatever that is.
  - **What is the maximum contribution rate that you would be prepared to pay for your benefits?**

What's <u>not</u> good about the UPP for employees?

- **<u>Sustainability</u>**
  - No proposal for scientific risk management.
  - No projections of potential variability in benefits and contributions.
  - Conditional inflation protection means there may be decades with no inflation adjustment of benefits in payment.
  - Overly generous benefits.

Comparison with other Ontario public sector JSPPs

Feature	UPP	OTPP	CAAT
Accrual Rates	1.6%	1.55%	1.3%
	2.0%	2.0%	2.0%
Early Retirement	60	~55	~55
Inflation Protection	75% of CPI Conditional	100% Conditional	75% Conditional
Member Contributions	~10.2%*	~11.5%	~13.3%

What's <u>not</u> good about the UPP for employees?

- **<u>Fairness</u>**
  - No attempt to address inherent inequity in pension design towards the higher paid
    - Two tier accrual rates.
    - No inflation protection for withdrawal pensions.
    - Poor inflation protection for retirees hits lowest paid disproportionately.
    - Final salary benefit is less fair than career average salary benefit.

Question 4

What's good about the UPP for employees?

What's good about UPP for employees?

- Generous benefits if it all goes well.
- Easy transfer between member universities
- May be better than the alternatives:
  - Perhaps a forced wind-up and transfer to a Defined Contribution plan.
  - Crippling future pension costs
    - Will impede universities' ability to fulfill core mission, potentially for many years.

Questions?