University of Waterloo Pension Plan  
June 2012 Information Sessions  
Responses to Frequently Asked Questions

1. **What is the deficit?**
   For the purposes of the presentations in June and this FAQ, the word “deficit” refers to the going concern deficit. The going concern calculation assumes that the plan will continue to operate for the foreseeable future. A going concern deficit occurs when the value of the liabilities (calculated using plan member data, the benefit structure of the plan, and actuarial assumptions) is greater than the market value of the assets. If a going concern deficit occurs in a year in which the actuarial valuation report is filed with the government (filing is required every three years), the university is required to pay down the going concern deficit within fifteen (15) years of the date of the valuation report.

   The going concern calculation is distinct from the solvency calculation, which assumes that the plan is being wound-up and the benefits accrued by plan members settled by purchasing annuities or making lump-sum payments. The costs associated with wind-up are built into the calculation, but the cost of indexing pension benefits after termination or retirement is excluded. If a solvency deficit occurs in a year in which the actuarial valuation report is filed with the government, the university is required to pay down the solvency deficit within five (5) years of the date of the valuation report, unless the government has agreed to extend the period.

   There is also a wind-up calculation performed in years when the university is required to file a valuation report. The wind-up calculation is similar to the solvency calculation, but it assumes that annuities will be purchased for members that provide for a 75% indexation benefit.

   The university’s last filed valuation (dated January 1, 2011) shows a going concern deficit of $141 million, a statutory solvency deficit/surplus of $0, and a wind-up deficit of $497 million. Based on this year’s valuation, the going concern deficit is now $170 million. (The other two numbers were not calculated, because the valuation report will not be filed this year.)

2. **What is the origin of the deficit?**
   The short answer, on which we will expand, is that the deficit is a product of the decline in the value of the pension plan’s assets and increase in the value of pension plan’s liabilities.

   The assets are made up of contributions by the university and plan members, which have been invested in the financial markets. The rate of contributions was set based on the assumption that the invested assets will earn 6.35% per year (including inflation). (Note: the assumed rate of return was reduced to 6.10% this year to reflect current and anticipated economic conditions.) With the collapse of the financial markets in 2008 and continued instability, the assets declined dramatically in value and have not recovered fully.

   The liabilities, on the other hand, have continued to increase, as new members join, existing members continue to accumulate service in the plan, and salaries, inflation and life expectancy
increase. The growing gap between the value of the assets and liabilities has produced the deficit we have today.

3. **Do we really have to pay down the deficit?**
   Yes, under the *Pension Benefits Act*, we are required to make annual payments towards paying off the deficit with interest within 15 years of the date of the last actuarial valuation report we filed with the government.

4. **Isn’t the deficit the university’s responsibility to manage?**
   Yes, however, in order to pay down the deficit, the university only has two options: (1) with the agreement of the Pension & Benefits Committee and the Board of Governors, make changes to the pension plan to reduce the cost of the obligations and/or increase contributions; or (2) increase the portion of the operating budget allocated to the pension plan each year. With respect to the second option, the university is already making additional payments to the pension plan, and cannot further increase its contributions – the budget for 2012/13 includes a small surplus; however, the surplus was achieved through expenditure reductions (as opposed to increases to income). The budget is expected to be further constrained over the next few years, as governments reduce funding to and expect greater efficiencies in the post-secondary sector.

5. **Why didn’t the Pension & Benefits Committee act sooner to address the deficit?**
   The committee continuously monitors and proactively takes steps for the health of the plan (whether the plan is in deficit or surplus). In late 2006 and early 2007, the committee undertook a review of the pension plan’s design. Based on the results of that review and after consultation with the community in April 2007, the committee recommended changes to the pension plan, which put the plan in a better position than others going into the economic downturn. As economic conditions worsened and the plan moved from a modest surplus to a large deficit, the committee continued to monitor and take steps to address the health of the plan: the committee recommended and the Board of Governors approved increases to contributions in 2007, 2008 and 2009, and modest reductions to non-core benefits in the spring of 2010. The financial markets started to recover and the position of the plan was improving in 2010; however, by the end of 2011, with the market volatility and renewed concerns re: Asian and European economies, the gap between the assets and liabilities started to grow again. So the committee has been taking steps all along, but due to factors outside of its control, the deficit remains and further changes are necessary. Please see a [summary of communications](#) to plan members on the foregoing matters from 2007-2012.

6. **Are there any Ontario university defined benefit pension plans that don’t have a deficit?**
   No. Most Ontario university defined benefit pension plans are struggling with a deficit. Because of the early action by the Pension & Benefits Committee to address the health of the plan (as described above), the University of Waterloo pension plan is in a better position than many other plans. The following are some articles on the state of university pension plans in Ontario and across Canada:
   - [Globe and Mail article](#)
   - [University Affairs article](#)
7. **How do the benefits and contribution rates of the UW plan compare to other Canadian university defined benefit plans?**

The UW pension plan is competitive with other pension plans, and in some cases, contributions are lower and benefits are better. Please see the following summary for a comparison of benefits and contributions rates of other Canadian university defined benefit plans: [Defined Benefit Plan Comparison Document](#). Further, other pension plans are in the process of making changes to improve their financial positions. Please see the following document for a summary of changes being made to university pension plans as of September 2011: [Summary of Changes to University Pension Plans](#).

**Please note:** the linked documents do not reflect the most recent recommended changes to the UW plan, as the documents were produced for the purposes of discussion prior to the recommendations being made and the changes have not been approved by the Board.

8. **Why can’t we wait to see if the financial markets improve?**

The financial markets are not expected to improve for at least three to five years. The pension plan needs to earn 6.10% per year in order to pay for the pensions earned by its members. Even if there is a modest improvement in the financial markets over the next three to five years, if the pension plan does not earn 6.10% every year, the deficit will continue to grow and more drastic changes will be required. In other words, we cannot afford to wait any longer to make these changes.

9. **Did the committee consider just increasing contributions or reducing or eliminating other benefits?**

Yes, the committee spent a great deal of time considering various options. This bundle of changes is being recommended, because it has the greatest impact on the funding of the plan without burdening one generation of plan members or employee group (faculty, staff, CUPE) more than the others.

The following analysis illustrates the impact of increasing contributions in lieu of reducing benefits. If the recommendations are approved by the Board, member contribution rates will be raised by **on average** 0.5% of salary. If the change to the final average earnings was made but member contribution rates were increased further rather than changing the indexation provision, member contribution rates would have to increase by an additional 1.0% of salary **on average** (that is, 1.5% of salary in total). If there were no benefit changes made, the total increase would be approximately 2% of salary **on average**. For some plan members, these increases may be a real financial burden, particularly in cases where the plan member’s increased contributions exceed the average. Further, if the increase in contributions alone is not enough to eliminate the deficit, plan members may still be subject to benefit reductions and/or further increases in contributions in the future, which creates generational inequity between these plan members and those who retired before the changes were made.
10. **What does the change in indexing imply?**

The pension benefit paid to you each month after you retire is set as the date you retire based on the pension formula. Under the University of Waterloo pension plan the pension benefit paid to you increases each year by 100% of the increase in the Consumer Price Index (to a maximum of 5%). The Committee is recommending a reduction in the rate by which the pension benefit increases each year from 100% of the increase in the CPI (to a maximum of 5%) to 75% of the increase in CPI (to a maximum of 5%) for pension accrued after December 31, 2013. The primary reasons behind this recommendation are that this change reduces the liabilities of the plan, and therefore, the going concern deficit, as well the indexing benefit is the easiest to increase or restore in the future. Please see the [Examples in Connection With Pension Plan Changes document](#) for some more information on the recommended change to indexing.

11. **If the legislation requiring 50:50 cost-sharing between members and employers is not yet in force, why is the committee recommending making this change now?**

The Committee is not making these changes in response to the direction the Ontario government set out in its March 2012 Budget. The changes are being made to address the funding shortfall in the UW Pension Plan and to ensure the long-term sustainability of the UW Pension Plan.

12. **Had the Committee already made the decision re: these changes before the information sessions in June? Or was feedback taken into consideration?**

The Committee did not finalize its recommendations to the Board of Governors until the Committee’s September 2012 meeting, after considering plan member feedback and additional information from the consulting actuary. The memo sent to the community at the beginning of October 2012 highlights changes to the original recommendations based on feedback from plan members. The recommendations are still subject to approval by the Board of Governors at the October Board meeting.

13. **If the deficit is paid down, can benefits be restored?**

With respect to reduction of guaranteed indexing from 100% to 75% of CPI, the Pension & Benefits Committee has committed to develop a protocol setting out the parameters under which the committee would be permitted to increase the level of indexing in the future. Once adopted, decision-making in accordance with the protocol would become part of the annual work plan for the committee.

With respect to the other benefits, they can be restored by amending the terms of the plan with the approval of the Pension & Benefits Committee and Board of Governors. Before approving an amendment of this nature, the committee and Board would need to be confident that the pension plan can afford the additional cost over the long term.

14. **What are the caps referred to in the presentation?**

The caps are maximum amounts of pension payable per year of credited service. Under the *Income Tax Act*, there is a maximum pension that can be paid from a registered pension plan. In 2012, the maximum pension is $2,646.67 per year of credited service. In addition, UW has a non-registered plan that increases the maximum pension in 2012 up to $3,031 per year of credited service.
service (the pension paid from the non-registered plan is the difference between these two caps, or $384.33 per year of credited service based on the 2012 amounts). In 2012, the combined maximum pension is reached at a final average earnings of $165,800.
The above maximum pension amounts are indexed each year by the increase in the average industrial wage, subject to a UW-specific cap of $3,200 per year of credited service. One of the recommended changes is to keep the UW-specific cap under the registered pension plan at the $3,200 level but to phase-in an increase in the cap under the non-registered plan to $3,400 per year of credited service. A maximum pension of $3,400 per year of credited service would be reached at a final average earnings of approximately $184,000.

Canada Pension Plan benefits are in addition to above amounts.

15. What happened to the surpluses we had in the plan previously?
There are two parts to this answer. First, the Income Tax Act previously required that pension plans increase benefits or reduce contributions if surpluses exceeded 10% of the value of the assets in a given year. The university did both during this period, although not to the extent of some other pension plans. Second, a surplus occurs when the value of the assets exceeds the value of the liabilities. As discussed under paragraph 1 above, the surplus we had at the beginning of 2008 was eliminated when the financial markets crashed, our assets declined in value, and our liabilities continued to grow.

16. What do you mean by the “pension promise”?
The pension promise is the promise to pay each member the pension earned by that member to date as calculated in accordance with the terms of the plan in effect when the pension was earned.

17. Will these changes impact existing retirees?
No. Existing retirees’ benefits are determined in accordance with the pension plan text in effect at the time their benefits were earned (pre-retirement). Protection for these benefits is enshrined in the Pension Benefits Act (Ontario).

18. Will these changes impact my entire pension or only the part earned after the changes have been brought in?
The changes being discussed now will only impact benefits earned by members after the changes come into effect. The benefits members earned prior to the effective date of the changes cannot be altered, as per the Pension Benefits Act (Ontario).

19. How is the pension fund invested?
The pension fund is invested in a variety of assets: Canadian and global equities, bonds, and more recently, alternative investments, such as infrastructure funds. For more information on the fund’s investment philosophy, asset mix, return expectations, benchmarks and investment management guidelines, please see the Statement of Investment Policies and Procedures.
20. Who manages the pension plan’s investments?
At the university, oversight for the pension plan’s investments is provided by the Pension & Benefits Committee, Finance & Investment Committee, Finance & Investments Subcommittee and Registered Pension Plan Investments Subcommittee, in consultation with our advisors at Aon Hewitt. The assets are held and managed by professional investment firms. The Registered Pension Plan Investments Subcommittee has primary responsibility for reviewing investment manager performance and making recommendations re: new investments, changes to asset mix, and termination and hiring of new managers. The Registered Pension Plan Investments Subcommittee is made up of four members from Pension & Benefits and three members from Finance & Investment. All recommendations from Registered Pension Plan Investments Subcommittee must be approved by Pension & Benefits and Finance & Investment, and in some cases, the Board of Governors, before implementation.

21. Are there limits on the types of assets in which a pension plan can invest?
Yes, there are limits set out in the pension legislation. There are also limits in the Statement of Investment Policies and Procedures.

22. Is the government going to merge our plan into other public sector plans?
It is difficult to predict what the government will do. However, it appears that the government is now focusing on options for co-investment of Ontario pension plan assets.

23. How likely is it that the government is going to force us to convert to a defined contribution plan?
As mentioned above, it is difficult to predict what the government will do. However, it appears that the discussion around defined benefit plans has shifted to how to make them more sustainable, rather than how/when to convert them into defined contribution plans. If the financial health of defined benefit plans does not improve overall, then the pressure to convert to defined contribution plans will likely resurface.

24. Will these changes affect my RRSP room?
No, these changes will not affect your RRSP room.

25. Has the impact of the aging population at UW been taken into account in these recommendations?
There are currently more active members than pensioners in the University of Waterloo pension plan. The university continues to grow and it should follow that the number of active members will continue to grow. As a result, we are not expecting to have a situation where there are more pensioners than active members at the University of Waterloo any time in the near future.

26. Could this all happen again in five years?
The intent of these changes is to make the plan sustainable for the long term; however, it is impossible to say whether the economic environment in which the university operates and the financial markets in which the assets are invested will improve or worsen.
27. How will the change to the final average earnings calculation impact members who entered into agreements with the university to forego a certain amount of vacation time in exchange for higher salaries before retirement?

The committee discussed this issue at its September meeting and will be recommending to the Board that for any member who has entered into a 2% salary increase in lieu of vacation arrangement with the university effective December 31, 2012*, the FAE calculation at his/her declared retirement date remain a 3 year average even if retirement is after January 1, 2014.

*Please note: Due to holiday closures, the last business day of the year is December 21, 2012. Forms need to be received by Human Resources prior to that date in order to be processed by December 31, 2012.

28. Is the inflation assumption reasonable?

Yes. The inflation assumption is 2.25%. For the past 20 years, inflation has averaged 2% per year.

29. Is the mortality table accurate given what we have been hearing about health issues in the media?

The change to the mortality table reflected in the January 1, 2012 actuarial valuation is based on the new table essentially becoming the standard for actuarial valuations. The new table reflects the continued improvement in pensioner longevity both to date and into the future. The experience to date has been evidenced in the actuarial valuations which show that current pensioners have been living longer than expected under the mortality tables used for the valuation. The improvements in mortality rates are expected to continue into the future and in fact recent analysis suggests that the rate of improvement in the current tables may be understated.

30. Is it reasonable to expect to get 3.85% (real) or 6.1% (nominal) return on investments?

The assumed future investment return is a very important factor is assessing how much of the pension benefits can be funded from investment earnings and how much will have to be funded by member and University contributions. The decline in interest rates over the last 10 years and the slowdown in economic growth in the developed economies has meant that the 3.85% real rate of return has become more difficult to achieve. So yes there is risk that the pension fund will not achieve that rate of return and that is reflected in the Committee's view that changes in contribution and benefit levels are required for long-term plan sustainability. At the same time, the Committee is focused on ways to try to achieve that investment return such as the recent decision to invest a small amount of the pension assets in public funds that invest in infrastructure projects.

31. Will the pension estimator on the Human Resources website be updated to reflect changes made to the plan?

Yes. After the Board of Governors meeting in October, Human Resources will engage the company responsible for supporting the pension estimator software to make the necessary changes.