REPORT OF THE JOINT SFU/SFUFA COMMITTEE TO DEVELOP A RANK ORDERED LIST OF PENSION PLAN OPTIONS FOR SFUFA MEMBERS

May 2018

<u>Introduction</u>

As part of the negotiation of a first Collective Agreement between Simon Fraser University (SFU) and Simon Fraser University Faculty Association (SFUFA) in 2016, the Parties signed a Letter of Agreement (LOA) about the SFU Academic Pension Plan (attached as Appendix A). Although the SFU Academic Pension Plan started out as a defined benefit (DB) plan, it was converted in 1973 to a defined contribution (DC) plan into which the University pays roughly 10% of salary. Additional contributions from members are optional. There is a small legacy DB provision still in place for members who opted not to convert their benefits when the DC provision was introduced.

In recent years SFU began hearing concerns from SFUFA that the existing pension plan does not provide sufficient retirement security for its members. This issue was discussed extensively at the bargaining table for the first collective agreement after SFUFA was certified as a union, leading to the LOA referred to above.

In this LOA the Parties agreed to establish a joint committee to provide a ranked list of pension options for SFUFA members. The members of the Joint Committee are
David Broun (Physics)
Julian Christians (Biological Sciences)
Ali Dastalmachian (Beedie School of Business)
Mark McLaughlin (Ancillary Operations)
Judith Osborne (Criminology)
Barbara Sanders (Actuarial Science)

The Committee was directed to consider options such as membership in an existing defined benefit plan, or development of a defined/target/hybrid option or any other option "it deems worth exploration". It was given a budget to hire legal/actuarial expertise to assist it in carrying out its task. The Committee decided that it would issue a request for proposals (RFP) to a small group of pension experts and then select the proposal that best suited its needs after evaluating the proposals, interviewing the proponents and conducting reference checking.

The Committee was further instructed to prioritize the following **principles** in developing its recommendations:

a) A pension plan with a defined/target/hybrid benefit
b) A jointly trusteed governance structure
c) University contribution rates consistent with existing provisions
d) Relatively equal contributions (subject to any legislative restrictions) of plan members and the University
e) Mandatory enrollment for new Association Members and optional enrollment for existing members

f) A plan that, considering costs and demonstrable savings, can be achieved within costing constraints including, but not limited to government mandates and the University's ability to pay
g) A plan that minimizes risk to the University and, insofar as possible, limits the University's liability to employer contributions for annual service costs.

Prior to issuing the RFP, the Committee made a decision not to seek an evaluation of defined benefit options, including either stand-alone or existing DB plans. It was acknowledged by the Committee that there would be little appetite for SFU to open up the existing DB Plan for Administrative, Professional and Union Staff to academic staff or to set up a new DB plan, given the problems with the existing DB Plan for staff regarding costs, unfunded liabilities, risk and governance issues. Also, by this stage, there had already been some exploratory discussions with the BC College Pension Plan (BCCPP) about the feasibility of SFUFA members joining that Defined Benefit Plan. The College Plan administrators were receptive to those overtures, but indicated that there were two significant preconditions: that all SFUFA members would have to join the College Plan and that there would be significant transition costs attached to joining the plan in the range of $30 million. (A more accurate estimate has since been obtained and is discussed further below) This lump sum represents a high level estimate of the additional assets that would be required at transition so that the addition of SFU faculty to the BCCPP for future service only would not change the BCCPP's funded position, sustainable indexing or the member and employer contribution rate.

Given the above, the Committee concluded that it was not possible to reconcile the characteristics of a DB option with the Principles set out in the LOA, and therefore omitted it from the scope of work in the RFP.

<u>The RFP Process</u>

The call for proposals was sent to a closed group of consultants who had local and national expertise with pension plan design and implementation. Two robust proposals were received and evaluated. Ultimately, the Committee selected a team from Aon Hewitt under the leadership of Rosalind Gilbert. Amongst this team's many strengths, it had unique experience converting a DC Plan in British Columbia into a Target Benefit Plan for the BCGEU as well as having broad experience with pension plans in the post-secondary sector.

<u>Background</u>

With the downturn in the economy in 2008 and a prolonged period of low interest rates, pension plans have been subject to scrutiny worldwide. The major concerns are and have been managing costs and risks as well as governance models. In the private sector there has been a long-term migration to DC plans from DB plans. In the public sector, DB plans have taken on greater risk in the last 15+ years. There has been recognition that changes are necessary for these plans to be sustainable in the long term.

Within the post-secondary sector, a review of pension plans at Canadian universities indicated 3 models that are provided to academic staff (faculty members): DB, DC and Hybrid plans. In several provinces changes have been implemented to address the concerns regarding cost containment, risk and governance referred to above. Some universities have closed their DB plans to new hires who join a DC plan instead (Saskatchewan); some provinces have a single plan for the academic staff of all universities (Alberta and under consideration in Ontario), while in Nova Scotia, universities are now allowed to join the Public Service Superannuation Plan.

Within B.C. the College sector is covered by the College Pension Plan (BCCPP) that provides a DB pension to both academic staff and senior administrative staff at the colleges and the special purpose universities. In the Research University sector, the prevailing model is the DC plan (SFU, UNBC). UVic has a DC/Hybrid Plan and UBC has a DC plan that, on a grandfathered basis with respect to the limitations in the **Income Tax Act**, allows a self-managed variable rate annuity as a decumulation option. To date, there has been no discussion of or interest shown in having a single plan for the academic staff of the research universities.

<u>Aon Hewitt's Analysis of the LOA's Operating Principles:</u>

At the outset, the pension consultants retained by the Joint Committee indicated certain limitations in the operating **Principles**:

- There was some inconsistency between the principles, specifically, a DB or hybrid plan with a joint governance structure would not have decision-making aligned with risk; the cost limitations in the last two **Principles** may not be achievable if a new plan is for new hires only; and with a DB or Target Benefit plan, limitation of University contributions to current service cost only may not be possible.
- The **Principles** do not appear to consider an enhanced/risk-pooled DC plan.
- Optional enrollment for existing members may lead to anti-selection that could result in higher administrative costs to the University and reduced risk pooling.

The consultants then suggested some additional considerations to the Joint Committee:

- A new plan should be sustainable, i.e. "a plan that can consistently deliver, through both favourable and adverse circumstances, an appropriate range of benefits within an acceptable range of costs".
- Define target contribution levels for the University and for plan members.
- The possibility of having separate provisions/plans for past and future service.

- Consider the issue of integration with enhanced CPP contributions and benefits.
- Bear in mind pension accounting requirements, ongoing administration requirements and resources and governance.

Presentation of Pension Plan Options

At the outset, Aon Hewitt proposed four options for the Joint Committee to consider that were subsequently fleshed out and evaluated:

1. Revisit participation in the BC College Pension Plan
2. An enhanced DC plan
3. A target benefit plan
4. A university sector multi-employer plan

BC College Pension Plan (BCCPP)

Given that a DB plan option was omitted from the scope of work set out in the RFP, it was somewhat surprising that one of the first suggestions the pension consultants raised with the Joint Committee was the possibility of revisiting joining the BC College Plan as an option.

They pointed out that the BCCPP is a robust, jointly governed, cost-shared DB plan that at its last valuation on August 31, 2015 was fully funded on a going concern basis. It provides to Plan members a reasonably predictable and stable lifetime pension compared to the other options. While the contribution rate of approximately 10% of salary that is required from Plan members is high (roughly equivalent to the employer's contribution) it provides a benefit calculated as follows: 2% x (years of service) x (average of best five years' salary). Over the long term this would provide an improved pension benefit for SFU faculty members over the current SFU DC Plan.

In joining the BCCPP, decisions would need to be made whether the current SFU DC Plan could or would be wound down immediately or over time. There would be costs incurred in any wind down as well as costs incurred in communicating the transition to the BCCPP. At some point, however, SFU resources currently used in pension plan administration, communication, oversight and management could be freed up.

The Aon Hewitt consultants suggested to the Joint Committee that there might be an opportunity to have a more refined analysis undertaken of the transition costs and that it might be premature to exclude the BCCPP as an option before knowing those results. In light of this advice, the Joint Committee commissioned a detailed actuarial analysis of these transition costs, carried out by Eckler Ltd., the plan actuaries for the BCCPP. That analysis was completed and forwarded to the SFU joint committee on May 1, 2018.

Since Eckler's most recent actuarial report on the BCCPP was an August 31, 2015 valuation, the costing for the putative SFU transition was carried out assuming that it also took place on August 31, 2015, and was based on age/gender/salary data for SFU Faculty Plan members as of the same date. The costing of the transition was carried out in two parts: its impact on the funding position of the basic account (from which base-level pensions benefits are drawn, unindexed to inflation); and the impact on the separate inflation adjustment account (IAA), which funds inflation indexing in the post-retirement phase. (In the absence of data on future hires, no account was taken on the impact of future SFU faculty new entrants on the BCCPP plan valuation, which might arise if the age or gender profile of new SFU faculty members were substantially different from that of existing BCCPP members.)

In order to make the BCCPP basic account whole (i.e., maintain its 101.56% funded ratio as of August 31, 2015), it was determined that SFU would need to contribute a lump sum of $19,043,000 to the basic account at the time of transition. This could alternatively be amortized over 15 years, at a cost of 1.27% of total salary mass. While this is smaller that the initial estimate of $30 million, it still represents a substantial sum. However, when a sustainable-indexing-based valuation of the impact on the inflation adjustment account was carried out, it was determined that SFU's contribution to the IAA could be lowered by 0.57% of pay over the 15 year amortization period. In summary, the net, amortized cost of the BCCPP transition would be **1.27% - 0.57% = 0.7% of payroll**. In addition, SFU's local costs of administering the current DC plan would be reduced over time as the DC Plan was wound down. Nevertheless, it should be pointed out that the transition to a DB plan, even one with as strong a track record as the BCCPP, would expose the plan's sponsors (jointly the SFU faculty members and SFU as employer) to the risk of future contribution increases or benefit changes, as they would share equally in any unfunded liability incurred as a result of poor investment returns, demographic changes or cost increases.

There are other potentially problematic issues: the BCCPP remains adamant that they will only consider having SFU Academic Staff join their Plan on condition that all members join. There would be no optional enrollment for existing members as set out in the **Principles.**

The BCCPP's membership criteria are not an exact fit with the membership criteria of the SFU Academic Pension Plan. The BCCPP requires that senior administrators of the institution also mandatorily enroll in the Plan. This group of potential Plan members was not included in the revised costing of transition costs and there has been no analysis done on the effect this might have on the pension benefits of these members or on the SFU Staff Plan.

And, although the BCCPP is a jointly governed plan, there has been no discussion of what role SFU and its faculty members might have in that governance model, if any. As the pension consultants pointed out, it is entirely possible that joining this plan could mean that the University and the Association would lose control and decision-making power.

<u>**Enhanced DC Plan**</u>

The second option tabled for consideration was an enhanced DC plan that would see an employee contribution, at least for new hires, and perhaps phased in for existing members. There would also be embedded in this enhanced DC plan more decumulation options, such as variable rate annuities, in addition to existing group LIF/RRIF options. Adding a variable rate annuity decumulation option would allow for longevity risk pooling.

Unfortunately, although this type of decumulation option is currently under consideration by the federal government, the <u>Income Tax Act</u> does not currently permit it unless it has been grandfathered as part of a pre-existing DC plan. But, assuming the regulatory framework changes in the near future to allow it, this could be a very attractive option, as it would align well with the LOA's **Operating Principles**.

There would be minimal change in Plan design leading to simpler member communication, minimal impact on administration and no change in the current shared governance structure. It would not, absent the introduction of more decumulation options, provide members who are currently close to retirement the opportunity to improve their projected retirement income. This, however, is true for any of the options that were under consideration.

<u>**Target Benefit Plan**</u>

A Target Benefit Plan (TBP) is a shared risk model. A hybrid between a DB and DC Plan, a TBP accumulates defined contributions to collectively secure a target benefit for members in retirement. Contributions and benefits adjust over time depending on the plan's performance. Currently, the <u>Income Tax Act</u> restricts the operation of TBPs to multiple employer plans, although a relaxation of this restriction is apparently being actively discussed at the Federal level.

Although the SFU Academic Pension Plan is commonly thought to be a single employer plan, the Faculty Association as employer has employees who are members of the Academic Pension Plan. Consequently, it is possible that a TBP containing both SFU and SFUFA as employers may already satisfy the multiemployer requirement, although this would have to be confirmed with the regulatory authorities.

Under this scenario, it would be possible to establish a TBP for SFU faculty members with the goals of pooling investment and longevity risk and so improving the predictability of benefits and costs. There are no specific requirements under the BC pension legislation for the governance structure of a TBP, which would therefore permit a shared governance structure similar to the current arrangement.

An initial decision would have to be made as to how to treat past service before proceeding to the design phase. The design phase is estimated to cost $100,000, with implementation costs estimated at $150,000-$200,000. If an administration system needs to be built or customized for the new plan, that could cost an additional $150,000 or more. There would also be legal, audit and other fees, although the consultants do not anticipate that there would be any wind-up costs since the conversion would be done under the existing plan registration number. The annual ongoing costs of a TBP are relatively high: administration fees are estimated at about $150 per member and $100,000 for actuarial, governance and investment consulting.

It would be difficult to set up a TBP if current SFUFA members were to have the option not to join the Plan, as it would take a considerable period of time to build up an asset pool that could provide an improved pension benefit. If membership in the TBP were made mandatory, the asset pool would accumulate faster. However, the costs of transitioning in this multi-age cohort would be a hidden cost in a TBP that would have to be paid over time from contributions and/or investment returns, reducing the benefit formula. Further, because there is no contribution flexibility in a TBP, it is required, under BC pension regulations, that a TBP have a very sizable buffer fund (a Provision for Adverse Deviations) in order to be able to offer stable benefits. The need for this buffer reduces the benefit formula.

As the pension consultants pointed out, the risk profile of a TBP at inception is significantly different from that of a mature plan. The initial cost in a low interest rate environment may be prohibitive.

Another option presented by the pension consultants was the possibility of joining a pre-existing TBP, which would eliminate plan design and startup costs. Aon Hewitt led the first conversion in Canada of a DC plan to a TBP for the BCGEU in 2016. That Plan has now been renamed the BC Target Benefit Pension Plan (BCTBPP) and is actively contemplating expanded plan membership. It is not clear at this point what role any new members would have in the governance of this plan, if any.

As a relatively small and new plan, the BCTBPP faces the same hurdles to being able to provide an improved level of pension benefit as a stand-alone option for SFU. The benefit levels from the BCTBPP would be unlikely to represent an improvement for SFU faculty members. The contribution rates are 8% from the employer and 6% from the employee and the annual pension that is produced is 9% of total contributions.

Another potential issue associated with joining the BCTBPP would be differences in demographic profile such as mortality rates and employment patterns. This could result in persistent subsidies flowing from one group to another, which would undermine the equal sharing of costs and risks.

Research University Sector Multi-Employer Plan

The fourth option raised for consideration was the potential for a University sector multi-employer plan. Initially the Joint Committee was lukewarm to this proposal largely because there was no obvious interest at any of its sister institutions in pursuing such an option. However, in the course of discussions of an expanded DC Plan, it was pointed out that the UBC Faculty Pension Plan (UBCFPP) is a DC Plan with a variable rate annuity decumulation option that was grandfathered when the Income Tax Act was amended to remove them. In other words, the UBC Plan is a good example of the type of enhanced DC Plan discussed above.

UBC makes a contribution of the same magnitude as SFU makes into its DC plan for faculty (roughly 10% of payroll), and UBC faculty also make a contribution in the range of 5%. UBCFPP members can choose to invest their and the University's contributions in one or more of seven investment funds, including a Balanced Fund, which is the default option.

In retirement, UBCFPP members may choose to use all or a portion of their accumulated account balances to provide a variable lifetime annuity that incorporates mortality risk pooling. The lump sum amount that a plan member wants to use to purchase a monthly annuity is transferred into a retirement annuity account invested in the UBCFPP's Balanced fund. There are two options: a 7% annuity and a 4% annuity. If the annual return on investment exceeds the rate option selected then the benefit would increase the following year; if the return on investment were lower than the rate option selected, the benefit would decrease the following year. The current best estimates for the long-term net return are in the range of 5.5 to 5.75%.

The UBCFPP is governed by a jointly trusteed Board. It also already incorporates employers other than UBC, although most, if not all, have some kind of relationship with the University.

This raised the question of whether SFU might be able to join the UBC plan as a new participating employer. To date there has been no indication that this is something that UBC might consider and, even if it did, whether SFU and its faculty would be granted a meaningful role in the governance of the plan. In other words, there is a similar governance concern with this as a potential option as with joining the BCCPP or the BCTBPP. It should be noted, however, that in terms of demographics and career trajectory, SFU faculty are much more closely aligned with UBC faculty that they are to the members of the other plans. Certainly, some members of the Joint Committee were less concerned about this governance issue than others.

Ranked List of Plan Options

The Pension Plan Letter of Agreement directs the Joint Committee to produce a ranked list of plan options to the Parties. Having considered the options and analyses presented by the Aon Hewitt consultants, it is clear to the Committee that each option has strengths and limitations.

The BCCPP offers the most improvement in the pension benefit over the long term compared with the other options. Relative to the LOA's **Operating Principles**

- It would guarantee a reasonably predictable and stable lifetime pension to faculty members
- It operates on a shared governance model, but it is unlikely that SFU and/or its faculty would have a seat at the table
- University contribution rates are consistent with current provisions, but that could be subject to change
- Plan members and the University would make relatively equal contributions and
- There would be mandatory enrollment for new SFUFA members.

In addition to pension income, it would provide members with access to the BCCPP group health plan, which has substantially lower premiums and a higher lifetime benefit limit than the current group plan available to faculty members.

However, there are several potential barriers to joining the BCCPP. As pointed out earlier, joining the BCCPP would incur transition costs of the order 0.7% of payroll, for a period of 15 years. Additionally, the BCCPP insists as a condition precedent that all existing SFUFA members would have to join the Plan as well as SFU senior administrators who are not currently members of the SFU Academic Pension Plan. Finally, the strong track record of the BCCPP notwithstanding, there is exposure to economic and demographic risks (as there would be in any DB Plan) and it is unknown if there would be any active role for SFU or SFU faculty to play in the governance of the Plan.

IF the transition costs could be covered in a way that did not come into conflict with the **Principles**; IF SFUFA members would accept mandatory membership in the College Plan and the required employee contribution that would come with that; IF the requirement to include senior administrators could be satisfactorily resolved and IF the College Plan would accept SFU as a member with a meaningful role in the governance in the plan aligned with the risk that it would have to take on, then the College Plan would be the most attractive option. However, these are issues that must be carefully considered by all stakeholders.

The next most attractive pension model is the Enhanced DC Plan. It is similar to the existing Pension Plan for Academic Staff and therefore familiar to members and perhaps less likely to generate fears and anxieties that are often provoked by proposed changes to pension benefits.

Relative to the LOA's **Operating Principles**

- It would provide a reasonably predictable and stable lifetime pension, although not guaranteed in the same manner as a DB option
- A jointly trusteed governance structure would remain in place
- University contribution rates would be consistent with existing provisions
- It would be possible to have relatively equal Plan member and University contributions
- There would be mandatory enrollment for new SFUFA members
- Optional enrollment for existing Plan members is not recommended by the Aon Hewitt consultants, and with a model that is so similar to the existing Plan, there would likely be less resistance to mandatory enrollment for existing members
- An enhanced DC Plan can likely be achieved within costing constraints and
- It is a plan that minimizes risk to the University.

For the moment, however, the only step to enhance the current DC plan that is currently within SFU and SFUFA's ability to implement is the introduction of mandatory member contributions. This would significantly enhance the level of pension benefits for members, except for current members who are close to retirement.

Other steps to enhance the DC Plan must await regulatory changes that would permit expanded decumulation options to be added to the SFU DC Plan. The current shared governance structure could remain in place. The other variant of the decumulation enhancement would depend on UBC being willing to open up its Faculty Plan to other members, specifically SFU and to do so at a reasonable cost and with an inclusive governance structure.

The least attractive option is setting up a TBP or joining the BCTBPP as it would be unlikely to provide an improved level of pension benefit and would be costly to implement.

APPENDIX A

Pension Plan Letter of Agreement

Recognizing that retirement security is in the interests of both the University and faculty members, the parties agree to establish a joint committee (the "Committee") to develop recommendations to provide a defined benefit/target/hybrid pension option for SFUFA members.

The Committee will be comprised of three people appointed by the University and three people appointed by the Association, and will meet no less than biweekly.

The Committee may retain additional professional advice, the cost for such advice to be shared equally between the parties. All expenses of the Committee, except as specifically noted below, will be shared equally between the parties.

The Committee will consider the following options, and any others it deems worth exploration:

- application for membership in an existing defined benefit plan (for example, the BC College Pension Plan; the SFU Pension Plan for Administrative, Professional and Union Staff);
- development of a defined/target/hybrid benefit option either within the existing SFU Academic Pension Plan or a stand alone plan (see below);

In order to facilitate the work of the Committee, upon the signing of this Agreement, the University and the Association will select a legal/actuarial service to develop draft terms for a defined- and/ or target-benefit option within the existing SFU Academic Pension Plan or as a stand-alone option. This contract will be for a price not to exceed $60,000 and the University will pay this amount for this contract. The contractor will be directed to submit the draft report no later than September 15, 2016.

In developing its recommendations, the Committee will prioritize the following principles:

a) a pension plan with a defined/target/hybrid benefit;
b) a jointly-trusteed governance structure;
c) University contribution rates consistent with existing provisions;
d) relatively equal contributions (subject to any legislative restrictions) of plan members and the University;
e) mandatory enrollment for new SFUFA members and optional enrollment for existing members;
f) a plan that, considering costs and demonstrable savings, can be achieved within costing constraints including but not limited to government mandates and the University's ability to pay;
g) a plan that minimizes risk to the University and, insofar as possible, limits the University's liability to employer contributions for annual service costs.

The committee will take as a central concern the ability to introduce the chosen option no later than July 1, 2017. It is open to the Committee to suggest a different implementation date should there be good reasons for doing so.

The committee will provide a ranked list of plan options to the parties no later than October 31, 2016.

Before any option is implemented, it will require ratification by the SFUFA membership and by the Board of Governors.

It is the intent of the parties to have the new option in place by July 1, 2017. All deadline dates may be extended by mutual agreement of the parties.