

# COMMUNIQUE



September 23, 2008  
Volume 14, No. 1 - Page 3

## Possible Effect of Cost-of-Living Changes



- Mary retires on January 1, 2015, after 25 years of service
- 80% of Mary's pension (20 years) earned before January 1, 2010
- 20% of Mary's pension (five years) earned after January 1, 2010

Valuation shows no deficit

- Mary receives full pension amount **plus** 100% cost-of-living protection
- 100% on first 80% of her pension (earned before 1/1/2010)
- 100% on next 20% of her pension (earned after 1/1/2010)

Valuation shows deficit

- Mary receives full pension amount **plus** partial cost-of-living protection
- 100% on first 80% of her pension (earned before 1/1/2010)
- 50-100%\* on next 20% of her pension (earned after 1/1/2010)

Deficit eliminated

Valuation shows surplus

- Mary receives full pension amount **plus** 100% cost-of-living protection
- 100% on first 80% of her pension (earned before 1/1/2010)
- 100% on next 20% of her pension (earned after 1/1/2010)

When the Plan valuation shows a surplus after a period in which the cost-of-living adjustment has been less than 100%, pensions in pay will be adjusted to reflect the full cost-of-living adjustment. If there

is a sufficient surplus in the Plan in future, pensions in payment will be increased to the amount they would have been at if there had been no prior reductions in the cost-of-living amounts.

\* Percentage depends on amount of funding shortfall to be eliminated

### How does this change affect the Plan?

The Partners and the Plan also propose to modify the Funding Management Policy (FMP). The FMP provides some direction in terms of potential surpluses or deficits. As a result of making this change in benefits, the parties have determined that it will be possible to adjust a part of the FMP that affects the projected cost of future benefits. While the amendment in the FMP does not guarantee that there will be no deficits in the future, it reduces the risk of future deficits. In the event there is a future deficit, this amendment will help reduce the size of that deficit.

### How much of a risk is this for me?

After looking at several other mature defined benefit plans like ours that have made cost of living protection subject to plan performance, it is almost universal

that retired members have received full cost-of-living allowances. This is because of the adjustment that can be made in assumptions about the cost of future pensions. It is the goal to pay full cost-of-living protection as often as possible.

### Does this change affect current retirees?

No. If you are retired and already receiving your pension, your benefits and cost-of-living protection will not change, because your benefits are protected by legislation.

### Why was this solution selected?

As the Plan sponsors, the OTF and the Ontario Government have only two possible ways to balance the funding of the Plan—increase contributions or change benefits (or a combination of the two). To come to the solution, OTF, the Government and

# COMMUNIQUE



September 23, 2008  
Volume 14, No. 1 - Page 3

the OTPP, worked together to conduct extensive research on the assumptions used to value the Plan, the safeguards put in place by other Canadian pension plans of a similar size and maturity, and the preferences of working members. Based on this due diligence, we determined that further contribution increases would not be a sustainable way to address our funding challenge in the long term and that, of the benefit changes possible, the most palatable option among working members is to change the way post-retirement cost-of-living increases are determined when there is a funding deficit.

The proposed solution is similar to the solutions that have already been put in place for the Hospitals of Ontario Pension Plan and the Colleges of Applied Arts and Technology Pension Plan.

## *Why couldn't we just increase contributions?*

If we relied on contribution increases alone, we would need to raise contributions to more than 16% of gross salary, far beyond what teachers have indicated they would tolerate and beyond the 15% cap that we committed to at the last valuation. Over time, newer teachers would be shouldering the brunt of this and any future deficits through increasingly higher contributions. We did not believe this was an equitable solution.

## *What other options were possible?*

Other possible benefit changes considered were increasing the 85-factor to 90 or decreasing pension benefit levels by 10%. When we asked teachers which benefit change they would be most comfortable with should contribution increases alone be insufficient to address a funding deficit, most chose to make the amount of cost-of-living increases conditional on the health of the Plan—with the understanding that cost-of-living increases would resume in full once the Plan could afford it.

## *How does the Government pay its share?*

If there is a change required to the cost-of-living calculation in future due to a funding deficit, the Government will contribute an extra amount to the Plan—equal to the amount retired members did not receive as cost-of-living increases that year. In this way, the Government will do its part to reduce the deficit so that those affected will return to 100% cost-of-living protection sooner.

## *Will we still have a contribution increase in 2009?*

Yes, but it will be the expected 0.8% increase implemented to eliminate the 2005 funding deficit. There will be no change in contributions in 2010 or 2011.

## *How did we get here?*

In 2005, contribution rates were increased to eliminate a \$6.1 billion deficit in the last funding valuation. In that deal, the OTF and the Government also agreed to:

- Cap contributions at 15%.
- If contributions reached the cap of 15%, consider changing benefits.
- Conduct a survey to determine member preferences in case of future deficits.
- Retain an expert panel to examine the actuarial basis used for valuations.

At that time, we told you that the cost of providing pensions was growing faster than Plan assets despite continued strong investment returns. We also warned that we could have a deficit in 2008.

Since the preliminary Plan valuation in January 2008 showed a funding deficit, your representatives and a sub-committee of the OTF Executive have been meeting with the Government and the Plan managers. We analyzed the options and discussed what we

# COMMUNIQUÉ



September 23, 2008  
Volume 14, No. 1 - Page 4

would need to do to ensure the filing—due to the FSCO on September 30, 2008—would be balanced.

Once the sub-committee reached agreement on the solution, it reported to the Executive. The OTF Board of Governors was then convened to hear the details.

### *Why are benefits changing?*

It was our greatest hope that we would never have to make the changes to the Plan. However, after carefully reviewing all the options, we believe that changing the way we calculate post-retirement cost-of-living increases, when needed to address a deficit, is the most palatable solution. It will ensure we keep contributions under the 15% cap and is in keeping with members' feedback on the change they would prefer should it become a necessity.


### *What are the next steps?*

We will reconvene the Board of Governors on September 29, 2008 to seek its support of the agreement. The valuation will be filed with the FSCO by the September 30, 2008 deadline. Between now and March 2009, OTF, the Government, and the Plan managers will work out the precise mechanism for calculating cost-of-living increases during funding deficits.

Going forward, a new Partners' Advisory Committee will meet quarterly to share information regarding Plan economics and the actuarial assumptions.

Additionally, a mechanism is being put into place to allow a review of the assumptions used for the OTPP. The setting of assumptions is a critical process. The OTPP Board has a fiduciary responsibility to oversee the management of the Plan, including operations, investment, strategy and the projection of the Plan's liabilities into the future. At times, one or both Partners have questioned whether the assumptions used by the Plan were too conservative.

The establishment of an on-going committee to share information about all aspects of the Plan will ensure your teacher representatives and your Government partner are well informed and we will have additional opportunities to share our views and provide input to the Plan through this process.



We will continue to keep you informed as details are finalized. If you have any questions, please contact OTF's Director of Pension & Economic Affairs or your Affiliate pension officer.