TORONTO

STAFF REPORT
ACTION REQUIRED

Metropolitan Toronto Pension Plan – Actuarial Report as at December 31, 2011

Date:	May 3, 2012
To:	Government Management Committee
From:	Treasurer
Wards:	All
Reference Number:	P:\2012\Internal Services\ppeb\gm12001ppeb (AFS15710)

SUMMARY

This report submits the Actuarial Valuation as at December 31, 2011 for the Metropolitan Toronto Pension Plan (the Plan) and recommends no cost-of-living increase for pensioners for 2012.

The 2011 Valuation sets forth the financial position of the Plan for the year ended December 31, 2011 on both a going concern and solvency basis and confirms that the Plan does not require any special payments by the City of Toronto.

RECOMMENDATIONS

The Treasurer recommends that:

1. City Council receive the “Report on the Actuarial Valuation for Funding Purposes as at December 31, 2011” prepared by Mercer (Canada) Limited with respect to the Metropolitan Toronto Pension Plan.

2. City Council confirm that given the deteriorating financial position of the Plan, the *ad-hoc* cost-of-living increase recommended by the Board of Trustees of the Metropolitan Toronto Pension Plan not be approved.

Financial Impact

There are no financial implications arising from this report.

The Deputy City Manager and Chief Financial Officer has reviewed this report and agrees with the financial impact information.

DECISION HISTORY

The Actuarial Valuation Report of the Metropolitan Toronto Pension Plan ("the Plan") is submitted annually to Council. The last such report was considered by City Council at its meeting held on May 17, 18, & 19, 2011, when it adopted Government Management Committee report GM3.7 "Metropolitan Toronto Pension Plan – Actuarial Report as at December 31, 2010".

Following is the link to the report and decision document:
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2011.GM3.7

ISSUE BACKGROUND

Pension plans are governed by the *Pension Benefits Act* (PBA) and regulated through the Financial Services Commission of Ontario (FSCO). The FSCO is an arm's-length agency of the Ontario Ministry of Finance, which is responsible for the administration and enforcement of the PBA and regulations under the Act. The PBA establishes the minimum standards for registered pension plans, and the regulations under it require the preparation and filing (at least every three years) of an Actuarial Valuation Report on a pension plan's assets and liabilities in order to determine the funded status of the plan on both a going-concern basis and a solvency basis.

<u>Going-concern valuation</u>: This type of valuation basis assumes that the plan will be ongoing for an indefinite period of time, and compares the value of the plan's assets as at the valuation date with the actuarially-calculated present value of all future liabilities as at the same date, yielding either a funding excess or a shortfall. The Valuation Report also contains a reconciliation with the excess or shortfall shown in the previous Report as a measure of the plan's financial health. An unfunded liability on a going-concern basis must be eliminated by the employer by one or more special payments, which may be amortized over a period not exceeding fifteen (15) years.

<u>Solvency valuation</u>: This type of valuation basis assumes that the plan was wound up on the Valuation date with all amounts coming due (*i.e.*, as if its assets had been used to meet its existing liabilities, including the purchase of annuities for its pensioners and unretired members). If a plan had greater assets than liabilities on a solvency basis on the Valuation Date, it has an actuarial surplus. If there were more liabilities than assets the plan has a "solvency deficiency" and, in order to comply with the PBA, that deficiency must be eliminated by the employer by one or more special payments which may be amortized over a period of no longer than five (5) years.

Actuarial valuation reports must be filed with FSCO and the Canada Revenue Agency (CRA) at least every three (3) years, unless at the end of any year the plan has a going concern unfunded liability, or a solvency deficiency in excess of 10% (*i.e.*, the plan is less than 90% funded) in which case such a report must be filed each year, until the deficiency is eliminated.

Asset Mix and Investment Returns

Given the demographics of the plan members, the Board of Trustees invest the Plan's assets conservatively in a well-diversified portfolio of equity and fixed-income securities. The Board monitors the investments prudently, with advice from its investment advisors, which it retains, in accordance with a Statement of Investment Policies and Procedures, which it reviews annually. The target mix of the Plan as set out in the Statement of Investment Policies and Procedures is as follows:

Asset Mix	
Cash & Equivalents	5%
Bonds	45%
Canadian Equity	25%
U.S. and Other Foreign Equity	25%
TOTAL	**100%**

The 2011 market rate of return was 2.39%.

COMMENTS

The Metropolitan Toronto Pension Plan ("the Plan") is one of five pre-OMERS plans sponsored by the City of Toronto. It covers 3 active members, 1,633 retired members and 1,011 survivor pensioners and 4 members with vested deferred pension rights. The Plan's administrator is the Metropolitan Toronto Pension Plan Board of Trustees ("the Board").

The Plan's Actuary, Mercer Human Resources Consulting, conducts an annual actuarial valuation of the Plan's assets and liabilities and recently submitted to the Board of Trustees its actuarial valuation for 2011. The purpose of the valuation was to determine:

(a) the financial position of the Plan as at December 31, 2011 on both going-concern and solvency bases; and

(b) the minimum funding requirements by the City during the 2012 calendar year, if any.

Going-Concern Valuation

The Valuation shows that at December 31, 2011, the Plan had actuarial assets of $512.1 million, liabilities of $457.8 million and a going-concern surplus of $54.3 million. The going-concern excess has decreased by $15.4 million (from $69.7 million at December 31, 2010). This is primarily the result of the cost-of-living increase provided in 2011 and decreased asset returns.

Solvency Valuation

As part of the Valuation, the actuary completed a solvency valuation comparing the Plan's assets at market value smoothed over four years with what it would cost to satisfy the Plan's obligation by winding up the plan and purchasing annuities using a discount rate that is also smoothed over four years. The report shows that on a solvency basis, the value of the assets was $504.7 million and the actuarial liabilities were $499.1 million, producing a solvency surplus of $5.6 million as at December 31, 2011. The previous valuation at December 31, 2010 indicated a solvency surplus of $30.2 million. This change in the solvency position is primarily due to the 2011 cost-of-living increase and losses resulting from the worse-than-expected performance of the assets.

Cost-of-Living Increase

The Metropolitan Toronto Pension Plan can be compared to the Ontario Municipal Employees Retirement System (OMERS) on the basis of plan design and municipal employee plan membership. However, while OMERS provides for automatic indexation, the Metropolitan Toronto Pension Plan does not. It could not afford to do so, because of its closed membership. Therefore, the possibility of a cost-of-living increase is reviewed annually as part of the Valuation Report in light of the financial position of the Plan.

The Board, at its meeting on April 27, 2012 approved the Actuarial Valuation as at December 31, 2011 and recommended that pensioners receive a cost-of-living increase of 1.00% effective January 1, 2012. The estimated cost of the recommended increase in pensioner benefits on a solvency basis would be $5.0 million and on a going-concern basis would be $4.6 million over the projected life of the Plan. The increase would be funded through the Plan without any contribution by the City. However, this would result in the solvency surplus being reduced from $5.6M to approximately $0.6 million.

Although providing a cost-of-living increase will not result in immediate funding requirements by the City, staff are concerned with the deteriorating financial position of the Plan. As indicated above, the Plan had a solvency surplus of $30.2 million at the end of 2010 which had deteriorated to $5.6 million at the end of 2011. Providing a cost-of-living increase, as recommended by the Board, would result in a further deterioration of the surplus to only $0.6 million. Given the turbulent market conditions and low interest rates, staff believe that exhausting the surplus by providing a cost of living increase this year would not be prudent. Should the Plan fall into a deficit by the end of the year, it would be the City's sole responsibility to fund that deficit, without any contributions from the pensioners or the single active member.

In addition, the Provincial Government has indicated its intent to disallow smoothing for the purposes of making the solvency calculation. If the Province does this, it would have a further negative impact on the solvency position of this Plan.

As has been the practice since amalgamation and prior to that in the former municipality of Metropolitan Toronto, the Actuary has, in view of the existence of a solvency surplus, made a recommendation for an increase to pensioners of 1%, the cost of which, on a solvency basis, would be $5.0 million and on a going-concern basis would be $4.6 million, leaving a solvency surplus of $0.6 million. That recommendation was made only in accordance with past practice and without any consideration of the market volatility of recent years or the possibility of a solvency deficit.

The Actuary also provided the Board with various projections on the financial status of the Plan at the end of the year, using various assumptions with respect to discount rates, asset returns and smoothing availability. Assuming that the Plan earns a 5.5% rate of return and that the discount rate is 3.5%, the Plan would have a solvency surplus of $9 million at the end of the year, if smoothing is allowed. If smoothing is no longer allowed, the Plan would have a solvency deficit of $9 million, resulting in an obligation by the City to make special annual payments of $2.0 million from 2013-2016 and $1 million in 2017.

As a result of the deteriorating financial position of the Plan, the potential that smoothing of liabilities may be disallowed and the actuary's projections indicating that the Plan may fall into a solvency deficit by the end of this year, staff cannot support the Board's request for a cost-of-living increase this year. In 2013, staff will evaluate the financial position of the Plan as at December 2012 to determine if there is sufficient surplus to fund a cost-of-living increase for pensions at that time.

CONTACT

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SIGNATURE

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Giuliana Carbone
Treasurer

ATTACHMENTS

Attachment 1: Metropolitan Toronto Pension Plan, Report on the Actuarial Valuation for Funding Purposes as at December 31, 2011 (April 2012)