

UNION PENSION SERVICES LTD.

92 Claremont Street, Toronto, Ontario M6J 2M5

December 7, 1999

Wilfrid Laurier University Staff Association
75 University Avenue West
Waterloo, Ontario N2L 3C5

Greetings:

RE: Review of Pension Documents – Control of Surplus

I have now completed my review of documents setting out the pension provisions for your members going back to September 1962 when the plan was first established.

THE 1962 PLAN

The original plan was created under Group Annuity Policy No. 7472 with Great West Life and required matching employer and employee contributions of 6%. The contract provided, in Section 25, for application of an "experience rating" toward reduction of the employer's contribution on an annual basis. I am not able to confirm the extent of such reductions, although for years prior to 1980, Annual Information Returns filed with the Financial Services Commission report employer contributions net of amounts labelled as "withdrawal credits". The amounts involved are small and decline to zero in 1980; these may be the amounts referred to in Section 25 of Policy 7472.

THE 1973 PLAN

The original 1962 Plan was revised and restated effective September 1, 1973. The 1973 Plan creates the money purchase accounts which continue to this day and provides for funds held in the 1962 Plan to be rolled-over into the money purchase accounts on the authority of individual releases signed by each affected member.

The "Preface" to the 1973 Plan Text states that, "Future contributions by the University will be equal to those made by members of the Plan, together with an amount sufficient to fund the cost of the guaranteed minimum benefit at retirement. Section 4.04 clarifies the employer's obligation to contribute.

"The University shall contribute annually an amount equal to the total of the required contributions of members of the Plan during the year, *and shall in addition contribute* such amount as is certified by the Actuary as appropriate to make provisions for the funding of benefits to be provided from the Minimum Guarantee Fund. (*italics added*)

The key phrase in Section 4.04 is "and shall contribute **in addition**". It is only the **additional** amount required to fund the supplementary portion or defined benefit guarantee which is based on the opinion of the actuary.

There is no suggestion or even implication that the matching contribution is subject to anyone's opinion or that it could be covered by surplus which might develop in the Minimum Guarantee Fund. The employer's obligation to contribute the matching amount is not conditional upon any circumstance other than a contribution being paid by the employee. The language effectively excludes the use of surplus to fund a contribution holiday on the money purchase portion of the plan because the University has no option but to contribute, in each year, an amount equal to employee contributions. The careful language concerning the "total" of contributions made by persons who were members "during the year" excludes even the possibility that the employer might not contribute the matching amounts with respect to members who left during the year without vesting of the employer's contribution.

The 1973 Plan Text contains no provisions which address, either directly or indirectly, the use of surplus in the Minimum Guarantee Fund while the plan is ongoing. The language of 4.04 concerning the Actuary's certificate has been interpreted by the courts as permitting the use of surplus to cover employer contributions. In this case, that well-established interpretation would apply only to the **additional** contribution to the Minimum Guarantee Fund.

The 1973 Plan Text does contain clear-cut provisions concerning the distribution of surplus in the event the plan is wound-up. Section 15.02 explicitly states that the University "shall not be able to recover any sums paid" and that the assets of the trust fund will be applied to the benefit of members.

The language of Section 15.02 was first modified by an amendment (no. 2) effective January 1, 1980. The amendment limits the amount of benefit payable on wind-up to Revenue Canada maximums. Any surplus remaining once those limits are reached is appropriated by the employer. The Income Tax Act and Revenue Canada rules would have permitted a direct cash payment to affected members of any surplus beyond the limits.

THE 1988 PLAN

The language concerning the employer's obligation to contribute is essentially unchanged in the 1988 Plan Text; the basis of the matching contributions is simply shifted to monthly from annually. However, there are more substantial changes to the provisions concerning surplus on wind-up.

The new provisions determining the distribution of surplus on wind-up are contained in Section 15.03 and provide that only amount of pension earned for service to the date of plan termination will be paid to plan members. All surplus remaining after these benefits are provided reverts to the employer. Under the amendment effective January 1, 1980, surplus would have been used to provide increased benefits up to the Revenue Canada limits and only the balance of surplus still remaining would have reverted to the employer.

THE 1993 PLAN

The language concerning the employer's obligation to contribute is changed by the addition in Section 15.05 which **requires** that surplus be used to reduce employer contributions and allows for the possibility that surplus would actually be withdrawn from the fund. The language concerning the distribution of surplus on wind-up is unchanged.

ADDITIONAL OBSERVATIONS

The plan was first amended to permit contribution holidays effective January 1, 1993. Surplus was first applied to reducing the employer's contribution in the plan year 1993/94; the employer's contribution has been fully paid from surplus in every subsequent year. The record of contribution holidays as recorded in Annual Information Returns filed with the Financial Services Commission follows:

Plan Year	Credit from Surplus
1993/94	\$1,288,736
1994/95	\$2,392,446
1995/96	\$2,431,156
1996/97	\$2,249,031
1997/98	\$2,241,432
1998/99	

Please note that there was an exceptionally low amount of employer contribution in 1973/74—\$162,581 versus \$237,724 by employees. This may have something to do with the transition to the new plan in 1973.

THE SCALE OF THE SURPLUS

The scale of surplus at stake is limited by comparison with the typical circumstances in pension plans generally. The reasons for this are the plan's reliance on money purchase accounts for active members and the direct participation of retired members in investment returns. The strong performance of the money purchase accounts in recent years leaves a small balance of liabilities for the Minimum Guarantee—approximately \$4 million.

The liabilities of the Minimum Guarantee Fund (or Supplementary Pension Fund) are most recently reported at page 5 of the actuarial report

as of July 1, 1997. Several relatively minor items totalling just over \$4 million leave a balance or surplus of slightly more than \$17 million. The actuary has acknowledged that the total amount of surplus is actually \$20.2 million, as noticed in my report of June 10, 1999. It is not yet clear whether the difference is also attributable to the Supplementary Pension Fund.

It should be understood that the Minimum Guarantee Fund is subject to a significant risk that its liabilities could increase dramatically in the event of a precipitous decline the market value of the money purchase accounts. New liabilities with respect to retired members would also be created if the guaranteed benefits with inflation adjustments exceed the variable pensions. It would be prudent and reasonable for the University to insist on maintaining a significant reserve against these contingencies. That reserve might be as much as 10% of the total of liabilities in the money purchase component and for the Minimum Guarantee—or approximately \$10 million. There is no obvious need for any additional reserve with respect to retired members in the current economic circumstances.

These considerations leave a balance of about \$10 million that could be available for benefit improvements and/or for contribution holidays. This balance might be augmented by the accumulated value of any past contribution holidays which were taken without being authorized by an agreement. In any event, it is apparent that the scale of surplus leaves only limited scope for contribution holidays. The matching contributions from the employer and the employees exceed \$4 million per year. It should also be understood that there is no basis for expecting that surplus would increase beyond its existing scale, there being only \$4 million of liability in the Minimum Guarantee Fund which could be reduced by further growth of the money purchase accounts.

CONCLUSION

The original language of the 1973 Plan concerning the employer's obligation to contribute leaves no room for alternative interpretations; the matching contribution must be deposited into the fund using monies from outside the fund. WLUSA has entered into agreements which provides for

contribution holidays during limited periods. You will want to confirm with those who were directly involved that there was no agreement in negotiations to modify the employer's access to surplus on an ongoing basis. Subject to this confirmation, I see nothing to suggest that the employer had the power to make amendments of the nature discussed in this report.

The language concerning the obligation to contribute does permit the employer to use surplus to reduce the contributions which would normally be required to fund the Minimum Guarantee Fund, but these are only a small portion of the employer's total obligation. The employer was permitted by agreement during certain periods to take a contribution holiday. It should be understood that, upon the expiry of any such agreement, the original terms of the plan would be restored.

The amendments to provisions in Section 15 concerning the distribution of surplus on wind-up has had no practical effect. However, the addition of Section 15.05 explicitly requires contribution holidays for the employer and has served as the authority for this ongoing practice. The same section also permits withdrawal of surplus from the fund. While you will naturally want the original language restored, it is unlikely that the provisions governing surplus on wind-up will have any practical consequence and there are only limited amounts of surplus available for further contribution holidays or benefit improvements. In any discussions concerning these issues, I would be inclined to put at least as much emphasis on maintaining and improving the Minimum Guarantee.

If the rate of matching contributions is increased for the future, the risk that money purchase accounts would fall short of the Minimum Guarantee would be correspondingly reduced. We might then consider that the special reserve was no longer necessary and that the full amount of surplus could be distributed in contribution holidays and benefit improvements. A package of early retirement incentives would be a natural use for such funds.

I would, of course, be happy to respond to any further questions which may arise from this report.

Yours very truly,

A handwritten signature in cursive script that reads "Don Lee". The signature is written in dark ink and is positioned above the printed name.

Don Lee

✓ cc: B. Switzman