Eckler
CONSULTANTS + ACTUARIES

Ontario Public Service Employees Union
CONFIDENTIAL

Eckler Ltd.
110 Sheppard Avenue East, Suite 900
Toronto, Ontario M2N 7A3
Canada

www.eckler.ca

Writer's Tel 416 696 3020
Email chunter@eckler.ca

March 8, 2018

Kim Macpherson
Benefits Officer
Pension & Benefits Unit, OPSEU
5757 Coopers Avenue
Mississauga, Ontario L4Z 1R9

Dear Ms. Macpherson:

Re: OPTrust Select

We have been asked to provide our comments on the sustainability report prepared on the OPTrust Select pension plan. OPTrust Select will be an upgraded career average pension plan with conditional indexing and no other ancillary benefits. Members and employers would each contribute 3% of pensionable earnings. This report will provide our comments based on the sustainability report provided and conversations with Dani Goraichy and Julie Belair of OPTrust.

Financial Management

It appears as if the OPTrust Select assets will be comingled with those of the OPSEU Plan. This is reasonable to achieve the advantages of investing in a large pool of assets.

We note that the conditional indexing of both earnings and pensions in pay will be based on the funded status of the OPSEU Plan. We would have expected that the conditionality would be based on the funded status of OPTrust Select. Based on our conversations with OPTrust, they noted that the intent will be to not have any cross-subsidization between the OPSEU Plan and OPTrust Select. The funding policy will address how to allocate deficiencies and surpluses equitably, and any experience gains or losses will be addressed by appropriate adjustments to the assumptions. Although this approach is expected to limit cross subsidies, there may be cross subsidies between the OPSEU Plan and OPTrust Select over short periods prior to any change in assumptions.

We suggest that consideration be given on the appropriateness of comingling all aspects of the financial management (e.g., investments and plan design) of OPTrust Select with OPSEU Plan or whether only the investments should be comingled.

We would assume that if OPTrust Select were operated with a separate accounting basis (i.e., a plan within a plan), that OPTrust Select would retain all of the advantages of jointly sponsored pension plan (in particular, that solvency funding would not apply).

Membership Data

The analysis is based on the OPSEU Plan active membership data. The demographics of the membership will influence the results. We cannot comment on whether this approach is appropriate or not, but suggest you consider the implications of membership that may have lower salaries, work part-time, may have different age profiles and may have a different gender split.

Discount rate
The report notes that "The nominal discount rate has been determined such that the present value of future contributions is equal to or slightly exceeds the present value of future benefits and related non-investment expenses where the benefits reflect earnings upgrades of 2.0% p.a. and post-retirement cost-of-living increases of 2.0% p.a."

The resulting discount rate from the above analysis was 5.6% p.a. In addition, the report notes that the above analysis was also prepared based on the Core Benefits, with the resulting nominal discount rate being 3.85%. Based on the information provided we are not able to verify this analysis.

A nominal discount rate of 5.6% seems reasonable to us, but we note that we have not reviewed the Long Term Acceptable Risk Portfolio.

Inflation
We note that the plan design is to provide active member upgrades based on increases in the Average Industrial Wage (AIW) and post-retirement cost-of-living increases based on the Consumer Price Index (CPI). The analysis has reflected earnings upgrades and post-retirement cost-of-living increases both at a rate of 2% annually. Appendix B notes that price inflation is assumed to be 2%, which is consistent with the analysis of the post-retirement cost-of-living plan design feature.

Appendix B also indicates wage inflation of 2.75% plus promotional scale (Table 1) was used to project future salaries. The implication is that although the career average plan design will control costs, the Intended Benefit growth (i.e. 2% p.a.) is expected to lag actual salary growth. Based on our discussions with OPTrust this was intentional and we're just identifying the difference.

Mortality
The sustainability analysis uses the same mortality table as the OPSEU Plan (i.e. 108% of CPM 2014 Private), with an adjustment to approximate the impact of an impending change to actuarial standards. This is a standard assumption. We are not able to comment on the appropriateness of this assumption without information of the demographics of the OPTrust Select membership.

Projection model
The sustainability report discloses that the results are based on one set of assumption (i.e. a deterministic approach was used). The report further comments that there is an 84% probability of sustaining the Core Benefits and only 57% of sustaining the Intended Benefits. We assume that these percentages are based on expectations from the asset modelling and not reflective of all of the risks that the OPTrust Select would face.

Sustainability analysis, in our opinion, would normally be conducted using a stochastic approach. That is, determine the impact of various factors changing. This is especially true when analyzing without any member data. For example, what is the impact if the average age of the membership of OPTrust Select is 5 years older or younger than that of the OPSEU Plan. What if the gender split is materially different? How important is different salary levels on the sustainability (and are there any correlations with other factors, like age)?

We agree that, if the percentages are based on the investment strategy, these outcomes appear reasonable. However, more detailed analysis may provide a better understanding of the impact of different demographics on the sustainability of OPTrust Select. We understand that OPTrust has prepared such detailed analysis and suggest that you request these results for your information on the potential risk points for OPTrust Select.

Advantages / Disadvantages
We were not asked to comment of the discussion of the advantages and disadvantages presented in the report. However, we concur with the observations made.

Conclusion

Based on our review of the sustainability report provided and conversations with Dani Goraichy and Julie Belair of OPTrust, we do not have any significant concerns or issues with the analysis prepared. We have identified that there are areas where additional information or further analysis would be beneficial in helping OPSEU better understand potential risks of OPTrust Select.

Our review was limited to the documents provided and a conversation with OPTrust. We understand that there are additional documents, such as a funding policy, that further address the objectives and approach to managing the plan that have been considered in the sustainability analysis. We have not provided any comments with respect to those details but recommend that consideration be given on their appropriateness.

Respectfully submitted,

D. Cameron Hunter, FCIA FSA

Cc: Domenic Barbiero, FCIA FSA, Eckler Ltd.

j:\opseu\pension\corr18\optrust select sustainability analysis comments.docx