PROVINCE OF NEWFOUNDLAND AND LABRADOR
HOUSE OF ASSEMBLY

HOUSE OF ASSEMBLY

MANAGEMENT COMMISSION

Technical Briefing | Wednesday, May 10, 2017

HANSARD

Speaker: Honourable Tom Osborne, MHA

The Management Commission met for a technical briefing at 5:15 p.m. in the House of Assembly.

MR. SPEAKER (Osborne): Okay, I think we are live and Broadcast is on, so we welcome any viewers who are watching. This is a technical briefing by the Department of Finance of the two options that are put forward for pensions for new Members: one that was brought to the Management Commission, the other through the MCRC.

The officials are Donna Brewer, Deputy Minister of the Department of Finance and Maureen McCarthy, Director of Pensions Administration, Department of Finance. I will ask them to identify themselves for the Broadcast Centre and for those who are viewing, and then I will ask Members of the Management Commission to introduce themselves as well.

On another note, prior to starting, this is a technical briefing and Members of the Management Commission are welcome to ask questions of the officials of the Department of Finance. The time for debate is the next Management Commission meeting. I won't entertain debate between Members tonight.

Other Members who are here to observe are here in that capacity as observers. If you have questions, I welcome you to write it on a piece of paper and pass it to a Management Commission Member. We won't entertain questions from observers tonight either.

We will start with the introductions.

Donna.

MS. BREWER: Donna Brewer, Deputy Minister of Finance.

MS. MCCARTHY: Maureen McCarthy, Director of Pensions and Debt Management, Department of Finance.

MR. SPEAKER: Okay.

And our Clerk, Sandra.

CLERK: Sandra Barnes, Clerk.

MS. KEEFE: Marie Keefe, Clerk's Office.

MR. SPEAKER: And we will start at the far end with Mr. Browne.

MR. BROWNE: Mark Browne, Placentia West – Bellevue.

MS. COADY: Siobhan Coady, St. John's West.

MS. DEMPSTER: Lisa Dempster, Deputy Speaker.

MS. MICHAEL: Lorraine Michael, St. John's East – Quidi Vidi.

MR. HUTCHINGS: Keith Hutchings, District of Ferryland.

MR. P. DAVIS: Paul Davis, Topsail – Paradise.

MR. SPEAKER: And I'm Tom Osborne, Chair of the Management Commission.

On March 15 this technical briefing was agreed to by the Management Commission on the provisions of the pension proposals put forward by the MCRC and one by the Government House Leader.

We will proceed at this point with the briefing by the officials from the Department of Finance.

MS. BREWER: Okay, thank you.

This is the outline of the presentation that Maureen and I will cover just to remind people of the current parameters governing the current MHA Pension Plan. We'll also discuss the recommendation that was put forward in the MCRC report. We'll then provide a comparison of the MCRC Defined Benefit recommendation with the Defined Contribution Plan that was presented.

We'll discuss the contribution rates and how they compare with the other provincial government public sector plans, and Maureen has an example there to further explain the difference from a financial implication for Members of a DB plan versus a DC Plan.

So we will start with the Current MHA Pension Plan. As Members will know, it is currently a

Defined Benefit Plan and that was first established in 1976. The current benefit structure is in place since 2009, and that is applicable for Members who were first elected to the House of Assembly after December 31, 2009.

As with all Defined Benefit Plans, there's a formula that establishes what the pension benefit would be and for this particular plan there's an accrual rate of 3.5 per cent, and you multiply that by the number of years of service and you multiply that by the average best three years' salary.

In contrast if I look at the Public Sector Pension Plan, which Maureen and I are a part of, we have a 2 per cent accrual rate, times our years of service. Right now for service since December 31, 2015 it's now on a best average six years.

This particular plan, there's a maximum service; you can contribute for 20 years. Thus, with an accrual rate of 3.5 per cent, your maximum benefit would be 75 per cent. Ministers' pensions are determined separately using the same formula but the ministerial salary gets added to the MHA compensation.

In this particular plan, a Member would vest after serving five years and after being elected for two General Assemblies; not eligible to draw the pension until age 55. For those elected since 2009, the 2009 group, there is a provision to retire earlier but there is an actuarial reduction of applied to the pension. At age 65, as with most Defined Benefit pension plans, this plan is integrated and the amount that you get in CPP will be clawed back from the pension benefit.

A deferred Member is a Member who is no longer sitting as a Member of the House of Assembly but who is not yet eligible to draw a pension. Right now, a deferred Member who is re-elected would qualify under the terms of the plan when they were first elected.

So here's an example now of how the current benefit is calculated for the MHA Pension Plan. This shows two examples: someone who had served for eight years and someone who had served for 12 years. The assumption is the average earning, the best average three years, is $95,357 and if the person is eligible for a pension from age 55.

So you can see there the pension for the person who has eight years of service is $26,700. When that person turns 55, there's a CPP reduction. So the person would get CPP but the person would also then get a reduced MHA pension of $24,065. The similar calculation is presented there for a person who sits for 12 years.

As indicated, a minister would earn a similarly calculated pension but you would add the ministerial salary and take into account the minister's service. The CPP reduction is only one reduction, so there would be no further reduction from the CPP.

MS. COADY: Can I just ask a question?

MS. BREWER: Sure.

MS. COADY: What's the current average for an MHA now, for years of service?

MS. BREWER: For years of service?

MS. MCCARTHY: The average salary?

MS. COADY: No, what's the current average term.

MS. MCCARTHY: The average term is just under eight years.

MS. COADY: So the eight- year figure? Okay, thank you.

MS. BREWER: There was a table, I think, in the MCRC report that talks about the percentage of people. The majority were – I think the medium was 7.6 years or something, and then –

MS. MCCARTHY: That's why eight is a good number to use in trying to get an example.

MS. BREWER: Yes.

Now, if we turn to the MCRC recommendation, the recommendation was for Members elected on or after November 30, 2015 that the annual benefit accrual rate would reduce from 3.5 per cent to 2.5 per cent; pension would be payable at age 60 versus at age 55. There would be no option to transfer service from other public sector pension plans. There will be no

indexation of retirement benefits. Maureen, there's no indexation –

MS. MCCARTHY: (Inaudible) now so it's nothing new.

MS. BREWER: There will be no changes to vesting or to survivor benefits. There was no specific comment that I could see about what happens to deferred Members.

As you recall, they're the Members who no longer sit in the House of Assembly but they're not eligible yet to draw a pension. There was no comment about what would happen should they at a future date apply and are successful and are re-elected. There's no ability to draw a reduced pension before age 60.

MR. BROWNE: Regarding the indexing, is the current MHA Pension Plan indexed?

MS. BREWER: No, it's not.

MS. MCCARTHY: No, it isn't.

MR. BROWNE: So she's not recommending a change there.

MS. BREWER: No.

MS. MCCARTHY: No. That's the –

MR. BROWNE: She's stating what is already status quo.

MS. MCCARTHY: Exactly.

MR. BROWNE: Thank you.

MS. BREWER: If we turn to the Defined Contribution, now as well, the MCRC report did have a Defined Contribution but it was a hybrid option. In the hybrid option, they had recommended a Defined Contribution Plan for the first eight years. Then if the Member chose to and was successful and presented themselves for a third time, they would qualify for a DB. But in talking with the actuary because, Minister Coady, based on your question, because the average tended to be around eight years, from a costing perspective there wasn't a significant difference between the hybrid proposal that was presented in the MCRC and the option that the Committee has asked to look at.

The MHAs under a DC Plan contribute a fixed percentage of salary and the government, the taxpayer, matches that contribution. Contributions are invested in the capital markets as directed by the MHA. That arrangement is consistent now with what we have in place for our part-time employees.

There's a Government Money Purchase Pension Plan which is a Defined Contributed Plan. It's administered by Great-West Life so there are various choices which we have to educate our Members on. It really depends on what your retirement objectives are, what your retirement goals are and your risk profile. You would advise Great-West Life in which type of capital market you would want to have the monies invested.

The major difference with the DC Plan versus the DB Plan is that your pension benefit is not known in advance and it's not guaranteed. So the value of your pension depends on the growth of that investment and how well the investment returns are within your particular fund. As I indicated, it cannot be predetermined in advance.

The funds that accumulate must be used to provide retirement income. Alternative use is not permitted. So it's not like a Tax-Free Savings Account where you can put the money in and withdraw it when you need it and it's also not like an RRSP as well where you can put the money in, get the benefit of the tax shelter, but then you can choose to take it out when you need it and be subject to tax.

The pension may be payable from as early as age 55 and the DC Plan is subject to the requirements under the *Income Tax Act* which governs the maximum contribution that can be made as well as the *Pension Benefits A*ct. The key thing with the *Pension Benefits Act* is right now the PBA standard for vesting is that Members vest after two years of planned participation.

MS. COADY: I'd like for you just to talk a little bit more about Member vested after two years planned participation because it has come up.

This is more like an RRSP plan? Is this similar to that?

MS. BREWER: It's similar but I would call it more of a locked-in RRSP because you can't withdraw the money.

MS. COADY: Okay.

You say the standard is to vest after two years. What does that mean?

MS. BREWER: If someone is elected and only serves a year, when they leave they only get the money that they put in. Whereas once two years pass and you're vested and you choose to leave the money is –

MS. MCCARTHY: The employer's share is yours as well.

MS. COADY: Okay, so it's the matched share would go to the individual.

MS. MCCARTHY: Yes.

MS. COADY: Okay.

Thank you.

MR. SPEAKER: Can I ask a question on that? I know my assistant, for example, is under a Defined Contribution Plan.

MS. BREWER: Okay.

MR. SPEAKER: My constituency assistant.

MS. BREWER: Yes, because the part-time employers and political support staff are under GMPP.

MS. MCCARTHY: And the political support are in this plan.

MR. SPEAKER: Yeah. There are some government employees who are under Defined Contribution now.

MS. BREWER: Right, yeah.

MR. SPEAKER: Some are under, I guess, a Defined Benefit Plan.

MS. BREWER: Right, yeah.

MR. SPEAKER: The government employees that are under Defined Contribution, how long is it before they're vested?

MS. MCCARTHY: Two years.

MR. SPEAKER: Two years as well. So this is no different than government employees that are vested.

MS. MCCARTHY: Employees who are in the Government Money Purchase plan are vested after two years.

MR. SPEAKER: Okay.

MS. MCCARTHY: The other plans are five years.

MR. SPEAKER: Okay.

MR. BROWNE: The other plans, you mean the other Defined Benefit Plans?

MS. MCCARTHY: Yes, the public service, teachers and uniformed service: the vesting is five years in those.

MR. BROWNE: And they would be Defined Benefit Plans?

MS. MCCARTHY: Yes.

MR. BROWNE: In terms of the Defined Contribution Plans that exist in the public service, is vesting after how many years?

MS. MCCARTHY: Two.

MR. BROWNE: And that would be consistent with this proposal?

Thank you.

MS. BREWER: Just to clarify though, when we were preparing the presentation, I did note that in the MCRC report they had referenced in the DC hybrid plan the same vesting for the DB Plan. We checked with the actuary in terms of the implications for costing and they said it wouldn't be a material change in the savings, one vesting over the other.

When we talk about the advantages and disadvantages of the Defined Contribution Plan you really have to look at the advantages from whose perspective. I guess from a taxpayer's perspective, the DC Plan doesn't have unfunded liabilities, the cost of the plan is known and it's the amount of annual contributions that the Member and then the taxpayer has to provide.

The disadvantages particularly for the Member would be the value of the retirement benefit is unknown. The Member is responsible for investment decisions and assumes all the investment risk. Now the plan will try to mitigate that because Great-West Life will offer education sessions.

What we find – because Maureen and I have both been involved with the GMPP, I'm a former chair – it's very difficult to get people to participate in these education sessions. I don't know, it especially tends to be part-time employees. It tends to be our younger employees in some cases. I guess retirement is probably the last thing on their mind but as two people who are close to retirement, 30 years goes by in a blink. My public sector announcement to young people is worry about your retirement now.

MS. COADY: One of the advantages, you said the cost of the plan is the amount of the annual contribution which is subject to the *Income Tax Act* and the *Pensions Act*. So currently, and I'll use our RRSPs, there's a maximum amount you can put in that's matched, right?

MS. BREWER: Yes.

MS. COADY: Okay. Thank you.

That's what I wanted to clarify.

MS. BREWER: The onus is on the plan sponsor to communicate the risks associated with the DC Plan.

MR. BROWNE: Your second point there under disadvantages: The Member is responsible for investment decisions and assumes all investment risks. Just so I'm clear and those who are listening are clear, under our Defined Benefit model, after your period of service if you're eligible, you get a set amount every year. Is that correct?

MS. BREWER: Yes.

MR. BROWNE: Under this proposal that might vary. Is that correct? It's not a set amount.

MS. MCCARTHY: It depends how you choose to utilize your retirement funds once you retire. Generally, you'd have a set amount. If you bought an annuity, for example, you'd have a set amount, but then if you chose some other way, just took it out into a Life Income Fund or a Locked-In Retirement Account where you could draw down certain amounts, it could vary.

MR. BROWNE: But that would depend on the Member making the decision on his or her own.

MS. BREWER: Maureen, under the GMPP, if I recall correctly, there's a default option that if people do not elect doesn't the money then go into a less receipt.

MS. MCCARTHY: No, actually in the current plan we have, if the employee doesn't make any choice with regard to their funds, the employer contributions will go to the balance fund and the employee's money will go to a one-year GIC.

MS. BREWER: Very low.

MS. MCCARTHY: Very low risk, but that was a decision made by the committee at the time.

MR. BROWNE: But the risk shifts from the taxpayer to the Member, is that right?

MS. MCCARTHY: Absolutely.

MS. BREWER: Yes, they have to be –

MS. MCCARTHY: The risk in a DC plan is definitely with the plan member.

MS. BREWER: I remember years ago someone told the story of two nurses hired on the same day; one went to the seminar, actively involved, managed their funds. One didn't, and they opened up their benefit statement one day and were shocked by the difference.

MS. MCCARTHY: By the difference in the accumulation.

MS. BREWER: The difference in the accumulation.

So, as indicated, the Defined Benefit Plan is the pension based on a prescribed formula. So the member doesn't have to worry about the markets and what happens in the markets. They don't have to worry about the actuarial assumptions of how long people are going to live and the survivors are going to live; all that falls to the worry of the taxpayer because they're the ones who have to pick up the extra cost if the actuary is wrong.

As we indicated, the value of the benefit is easily determined and is consistent with pension arrangements of full-time public sector pension plan members.

As indicated, the MHA DB Plan provisions, as recommended by the MCRC, was 2.5 per cent per year integrated with the CPP from age 65. The vesting hasn't changed, five years and two general assemblies. The average best three years wasn't changed at age 60 with five years of service, that's increased from age 55.

There has been no change to survivor benefits. So a member with a spouse, post-retirement death, 60 per cent of the member's pension goes to the spouse. Pre-retirement, the spouse has the option of taking the pension, the 60 per cent survivor benefit, or requesting the actuary to calculate the cumulative value and taking it as a lump sum. If the member dies and there is no spouse, there's a cumulative value paid to the estate.

In terms of the termination benefits; if not vested, refund of own contributions plus interest. If vested and not eligible for an immediate unreduced pension, the deferred pension is paid from the earliest eligible date. So under the new plan it would be age 60. Reduced pension would be eligible for people in the 2009 group or payment of the commuted value into a locked RRSP.

The advantage of the DB Plan for the member is that the pension is predictable and the plan sponsor is responsible for any investment of the contributions. As I indicated, then the taxpayer then assumes the risk. Disadvantages are that, particularly again for the taxpayer, costs can vary. They are susceptible to changes in plan demographics. If people live longer than the actuary had allowed for and whether or not the investment markets are doing good or – we've had some really bad hits in the last 10 years. Contribution rates accordingly are also susceptible to change.

Evaluations are done, Maureen, every three years?

MS. MCCARTHY: Every three years.

MS. BREWER: And the contribution rates could adjust depending on what the actuary says is the current cost of the plan and as a result of this, there are often unfunded liabilities. The unfunded liability, I understand for the MHA plan, is close to $90 million.

So if we look at the contribution rates, these are the contribution rates. These are the effective rates for the Public Sector Pension Plan. It works out to about 9.7 per cent. The next column, the current service cost is the actual cost that is shared 50-50 with the employer and the employee. So you can see there the employees true cost is roughly 7.55 per cent. So each employee is actually contributing over 2 per cent to help fund the unfunded liability.

Similar with teachers, the teachers' share is 8 per cent but they're contributing 11.35 per cent. So the balance goes towards the unfunded liability. The Uniformed Services are pretty much close to their share of the current service cost. Judges already went through the judges' tribunal and they did not recommend any change to that plan.

The MHA plan, you're at the maximum currently for the *Income Tax Act* of 9 per cent, and you can see there what the current costs are. GMPP, which is the Government Money Purchase Plan for part-time employees, the contribution rate is 5 per cent matched by the employer for a total cost of 10 per cent.

For the DC Plan, the maximum under the *Income Tax Act* is 18 per cent. That would be 9 per cent for the member and 9 per cent for government. Maximum total dollar limit for 2017 is $26,230. So that's the maximum that actually can be deducted on the tax return.

What we did then was we put all three side by side so you can readily see the differences between the current MHA plan, the MCRC Defined Benefit recommendation and the Defined Contribution.

Maureen, do you want to walk the committee through this slide.

MS. MCCARTHY: I guess what we tried to do here is just tried to compare the level of benefits that might be available to someone under both options. Basically, we looked at, for the DC side of it – we're trying to compare the DC to the DV. So the first column we would show the accumulation of funds under the DC Plan. What we did is we assumed the member had eight years of service and they would have 0 per cent increase in the first four years and 3 per cent increase thereafter; just to do that kind of projected salaries. They are first elected at age 40 and they worked for eight years.

These are actually taken directly from the MCRC report. If you look in the back of the Morneau Shepell Report, they actually showed some examples of how the DC – some of the pension that could be paid from the funds accumulated under the DC Plan.

So basically, across the first line we show the accumulated funds assuming different rates of return because obviously with a capital accumulation plan the rate of return on those investments is very critical to retirement income adequacy. So basically we assume the 4 per cent rate of return, 5.5 per cent annual rate of return and the 7 per cent rate of return.

We calculated the accumulated funds for both the member for eight years and for a Member and a minister over an eight-year period. Then from that, based on their chart, what was actually in the report, they determined what the annuity would be if you took those funds and annuitized them based on normal, I guess whatever they assumed in the actuarial evaluations, came up with what would be a reasonably expected level of income from those accumulated funds.

So, for example, in the first column, if the member had invested the contributions and had achieved 4 per cent rate of return they would have accumulated $267,239 and that would provide a lifetime annuity of $13,456 payable for their lifetime. We did that for the different return scenarios and then we just compared that to a member who was under the MCRC recommended plan as to what benefit would have accumulated under the Defined Benefit Plan after age 65, so that's in the third row. So you can see the differences there – and obviously, as the rates of return increase, the DC option looks better relative to the DB option, but again that depends on the success of the accumulated investments.

MS. COADY: You're suggesting – and I'm just trying to understand; there are a lot of numbers on this slide. Under – and I'll just use Member's Return Rate. So the first one is should my investments ever make 7 per cent in the market, I would have an annuity of $21,000 based on the fact that my employer would match my contribution. Is that correct?

MS. MCCARTHY: And if those were invested and you achieved that rate of return.

MS. COADY: Okay. So in today's environment, 4 per cent is a pretty great rate of return. So if my rate of return was 4 per cent, I would get $13,000 but under the MCRC, I would get $17,000?

MS. MCCARTHY: Correct.

MS. COADY: Okay, I just wanted to make sure I was clear.

Thank you.

MS. MCCARTHY: Just as a comparison, prior to pension reform of the Public Service Pension Plan, the annual objective was 6.75 per cent. It was a risky plan because we had invested a lot in the equities. After pension reform when the employees, the unions agreed to share in that risk with the taxpayer, they wanted to de-risk the plan, so the actual annual objective is a 6 per cent return.

MS. COADY: The objective is 6 per cent; what are we actually getting?

MS. MCCARTHY: The actual return as of the end of the March this year, the one-year return was 14.8 per cent on pooled pension fund.

MS. COADY: Oh, wow.

MS. MCCARTHY: But then if you go out over 10 years, which brings in the 2008-2009, the rate of return was 6.38 per cent premiums. It's all very sensitive to when you're actually measuring that stuff.

MS. COADY: Okay, thank you.

MS. BREWER: That's why it's an individual decision because if you're young and you can afford to wait for markets to return versus if you're like us and close to retirement, we don't have the years to recover. That's where your own individual plans and objectives and demographics would have to come into play.

MR. SPEAKER: Donna, a question: Regardless of the rate of return under the Defined Contribution, there's a risk, it could be lower than Defined Benefit or it could be higher than Defined Benefit.

MS. BREWER: Right, yes. There's no certainty.

MR. SPEAKER: There's no certainty, the Defined Benefit –

MS. BREWER: Whereas the Defined Benefit there is certainty.

MR. SPEAKER: – provides certainty to the Member but the Defined Contribution provides certainty to the taxpayer.

MS. BREWER: Right.

MR. SPEAKER: Is there a savings? If so, what is the estimated savings of one plan over another to the taxpayer?

MS. BREWER: Over the long term, it will result in the elimination of the unfunded liability.

MR. SPEAKER: The Defined Contribution Plan.

MS. BREWER: The Defined Contribution. So the existing Members and the existing pensioners – I'm sorry to be morbid, but once they die off and survivors die off and all you'll have left is the DC Members, there is no liability.

MR. SPEAKER: So the $90 million unfunded liability will eventually disappear.

MS. BREWER: It will disappear. But on an annual basis the two, roughly about a million dollars a year in savings.

MR. SPEAKER: Which would provide the greater savings?

MS. BREWER: Both were about the same from an accounting perspective. When I asked the actuary to give me extrapolations like, say, for government's seven-year plan, both of them were in the million-dollar range. From a liability perspective, the DC gives a better benefit to the taxpayer.

MR. SPEAKER: Okay, so when you say the DC gives a better benefit to the taxpayer, how?

MS. BREWER: Because there is no liability established for every new year of service for the DC Members.

MR. SPEAKER: So in the long run, will the DC save taxpayers money?

MS. BREWER: Yes.

MR. SPEAKER: Okay.

MS. BREWER: Because we go back, right now it will cost the taxpayers 9 per cent – I'm trying to get back to the contribution rates. Whereas the DB Plan –

MR. SPEAKER: Is 9 per cent, plus the unfunded.

MS. BREWER: If you look at the current cost of the DB Plan it was 42.5, of which half – well, more than half of that; 42.5 less 9 per cent is what the taxpayer is incurring.

MR. SPEAKER: And the Defined Contribution is simply 9 per cent.

MS. BREWER: Nine per cent.

MR. SPEAKER: Okay.

That's all the questions I have for the moment.

MS. BREWER: It will take a while before you see those accruals.

MR. SPEAKER: Before you see the savings.

I will open it to Members of the Management Commission for questions, should there be any.

Any other questions from Management Commission Members? I'll give an opportunity for the staff of the Department of Finance to make closing remarks.

MS. BREWER: We just appreciate the opportunity. Maureen is here until the end of June if you have any further questions. I'm still trying to figure out my date.

Thank you.

MR. A. PARSONS: Thank you.

MS. MICHAEL: Thank you very much. We appreciate your time (inaudible).

MS. BREWER: All right, thank you.

MR. SPEAKER: Thank you.

Mr. Parsons, before Management Commission Members leave, I did send out a request for a meeting next Wednesday. I've heard back from one Management Commission Member. I'm just wondering the availability of Members of the Management Commission for next Wednesday for a meeting.

MR. A. PARSONS: Can you send it again?

MR. SPEAKER: I can send it out again.

MS. COADY: The 17th?

MR. SPEAKER: That's correct.

MR. A. PARSONS: (Inaudible.)

MR. SPEAKER: Okay.

I will await your responses.

Thank you very much to Management Commission Members and officials, and that concludes the meeting.

On motion, meeting adjourned.