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Date: March 23, 2009
To: Governing Council Business Board Members
From: George Luste, President, University of Toronto Faculty Association (UTFA)
**Re: Agenda item #6. - Pension Plans: Annual Financial Report for the
Year ended June 30, 2008 – Revision**

The Issue: -

That revised guidance for 2008 has increased the rates from 40 basis points over Government of Canada bond yields to 110 basis points over Government of Canada bond yields, an increase of 70 basis points, to reflect deteriorating credit conditions.

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The impact for the University of Toronto Pension Plan (RPP) is a reduction in the solvency deficit from \$217.2 million to \$65.5 million,

Question: Is this deferring liability and thus increasing the *hidden* risk?

- (i) Background. As the attached table indicates, an actual wind-up solvency valuation of the UofT pension plan shows a deficit of \$1.1 billion as of July 1, 2008. This alarming liability is *hidden* for the time being by the fact that the provincial solvency test does not include the cost of the 75% indexation in our pension formula.

Since July 1, 2008 the market value of plan assets have declined substantially, resulting in a substantially larger deficit if the same evaluation was made today.

- (ii) Yield spread and pension liability. Because of the recent flight to safety in the bond market, and thus to Government bonds, yield rates on riskier corporate bonds have risen dramatically since the credit crisis began. The higher yields on corporate bonds reflect increased fear of default by the market.

Should pension liabilities be reduced because of diminished creditworthiness of annuity purchases? However the provincial solvency evaluation rules and CIA guidelines permit it.

- (iii) Filing. Given the provincial requirement that solvency filings must be made at least once every three years, the Administration's revised numbers and filing for 2008 means that the window until the next required filing has an extra year – until 2011. This delay provides more time for the markets to recover and thus also delays the legal need to deal with the pension plan problem.

- (iv) Short term decision. UofT Governors should understand that the current yield spread anomaly is almost certainly short term and will disappear – this revision, based on a temporary anomaly, is thus masking actual pension plan losses and so exposing the pension plan to added adverse consequences in the longer term.

Business Board: Conflict of Interest and Fiduciary Duty.

Question.

Does Business Board have an inherent conflict of interest in having oversight of both the university's finances as well as oversight of the pension plan and the interests of pension plan members?

This seems to be the classic “two-hat” problem.

Question.

Given the volume and complexity of financial responsibilities that Business Board must consider, does Business Board really have the time and expertise to provide proper fiduciary oversight of the pension plan?

UTFA believes that a change in pension plan governance is long over

Highlights¹

As at July 1, 2008

With Comparative Figures at July 1, 2007

BUSINESS
BOARD

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At July 1, 2008 (millions of dollars)			
	<u>Accrued Liabilities</u>	<u>Market Value of Assets</u>	<u>Market surplus (deficit)</u>
University of Toronto Pension Plan (RPP)			
Going concern actuarial valuation	2,889.6	2,724.2	(165.4)
Solvency actuarial valuation ²	2,940.4	2,723.2	(217.2)
Hypothetical wind-up actuarial valuation ²	3,862.2	2,723.2	(1,139.0)
University of Toronto (OISE) Pension Plan - RPP(OISE)			
Going concern actuarial valuation	104.2	105.9	1.7
Solvency actuarial valuation ²	108.7	105.5	(3.2)
Hypothetical wind-up actuarial valuation ²	140.6	105.5	(35.1)
Supplemental Retirement Arrangement (SRA)			
Going concern actuarial valuation	139.8	174.2	34.4

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→ (65.5)

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At July 1, 2007 (millions of dollars)			
	<u>Accrued Liabilities</u>	<u>Market Value of Assets</u>	<u>Market surplus (deficit)</u>
University of Toronto Pension Plan (RPP)			
Going concern actuarial valuation	2,745.8	2,929.7	183.9
Solvency actuarial valuation ²	2,628.4	2,928.7	300.3
Hypothetical wind-up actuarial valuation ²	3,441.6	2,928.7	(512.9)
University of Toronto (OISE) Pension Plan - RPP(OISE) - including partial wind-up			
Going concern actuarial valuation	115.3	131.6	16.3
Solvency actuarial valuation ²	113.9	131.2	17.3
Hypothetical wind-up actuarial valuation ²	142.9	131.2	(11.7)
Supplemental Retirement Arrangement (SRA)			
Going concern actuarial valuation	145.4	170.0	24.6

Going Concern Key Actuarial Assumptions	July 1, 2008	July 1, 2007
Increase in consumer price index (CPI)	2.5%	2.5%
Increase in salaries	4.5%	4.5%
Discount rate on liabilities	6.5%	6.5%

¹ Going concern valuations assume that the plan is continuing to operate for the foreseeable future. Solvency and hypothetical wind-up valuations assume that the plan will be wound-up as at the valuation date. See pages 10 and 11 for a full discussion of the different types of valuations.

² The market value of assets are net of wind-up expenses which are estimated to be \$1.0 million for the RPP and \$0.4 million for the RPP(OISE).