



An Examination of the Public Sector Pooled Pension Fund

NEWFOUNDLAND AND LABRADOR PUBLIC SECTOR
PENSIONERS' ASSOCIATION

Preliminary Results, October 2014

Final Report, February 2015

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NLPSPA

Newfoundland & Labrador
Public Sector Pensioners' Association

About the Report

The preliminary findings of this report were presented to the Newfoundland and Labrador Public Sector Pensioners Annual General Meeting (AGM) in October 2014. The Public Accounts and Auditor General's Reports for the Province were released later in 2014. This Final Report incorporates data and information from these new sources. It also addresses points raised during the AGM. The findings, results and essence of the report remains unchanged, it has simply been revised to reflect the most recent, readily available data.

About the Author

Alison Coffin, B.A. (Honours), M.A. Economics

Alison began her career as an Economist with the Advisory Council on the Economy, an independent think tank on public policy, in 1993. She has worked extensively within Government including the Departments of Education, Human Resources Labour and Employment and Environment and Labour. She became an independent consultant on a wide range of economic issues after leaving Government in 2004. Her experience is broad encompassing Provincial fiscal analysis, public sector pensions, labour market issues, program and policy development, federal presence in the Province, program evaluation, strategic planning, performance measurement, cost benefit analysis and small business development. Alison has taught Economics at Memorial University since 1997, including courses on the Newfoundland Economy. She is also a regular guest on Provincial and National media on issues relating to the Newfoundland and Labrador, Canadian and World economies.

Alison's previous work includes a study of the Past Government Actions on the Present State of the Pooled Pension Fund. The study found Government had agreed to provide pensions to its employees in 1967. These pensions were to be cost shared, with Government matching employees' pension contributions. Between 1967 and 1980, pension contributions deducted from employees were added to Government's general bank account and used to for things like roads and office furniture as well as pensions. Government did not match employees' contributions. This created a pay-as-you-go system where pension contributions were not saved for retirements and pensions owed were paid as they came due. If Government had instead created a pension fund in 1967, made matched contributions and earned interest on their deposits the Public Sector Pooled Pension Fund would have been worth \$4 Billion more that it was in 2010.

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AN EXAMINATION OF THE PUBLIC SECTOR POOLED PENSION FUND

Executive Summary

This report examines the structure, operation and management of the Province of Newfoundland and Labrador's Public Sector Pooled Pension (PSPP) Fund and the associated unfunded liabilities. It is intended to provide an overview of the Fund and its history to the members of the Newfoundland and Labrador Public Sector Pensioners' Association (NLPSPA).

The PSPP Fund was established in 1980 to finance benefits under the Government sponsored pension plans. The Minister of Finance is the Trustee of the Fund. The Pension Investment Committee advises the Minister on the operation and investment of the Fund.

Pensions are deferred wages. The PSPP Fund is designed to save and invest contributions to the Fund in order to pay these deferred wages (pensions) to the beneficiaries (the employees) in the future.

The NL Public Sector Pensioners' Association now owns the largest database of pension information available to the public. It is comprised of approximately 2,000 data points spanning 48 years (1967-2014).

The Public Sector Pooled Pension Fund is comprised of 5 pension plans. They are the pension plans of: the Public Service; Teachers; Uniformed Services; Members of the House of Assembly (MHAs); and Provincial Court Judges which was added in 2004.

The PSPP Fund generates annual returns sufficient to offset the value of pensions earned each year. (Pension Investment Committee, 2013)

- The annual average rate of return is 8.8%, more than 2% higher than the 6.75% annual return required.

Since 1991, about 99% of all employees' annual matched contributions to the Public Sector Pooled Pension Fund were sufficient to pay for the pensions earned by those employees. (Mercer, 2013) Current employees have been contributing enough into the PSPP Fund to pay for their retirement.

- If pension contributions had actually offset all pensions paid from the Fund since 1981 the PSPP would have \$7.8 Billion in assets and \$0 unfunded liabilities.
- This did not happen, instead the actions of Government have contributed to the growing unfunded liability in the PSPP Fund.

Only \$3.8 Billion, or 58%, of the \$6.5 Billion of the unfunded liability associated with employee future benefits can be attributed to the PSPP Fund. (Auditor General, 2014)

The PSPP Fund had \$489 Million in Unfunded Liabilities in 1981. If these liabilities had been addressed when the Fund was established there would have been an extra \$9.5 Billion in the Fund in 2014.

An analysis of the revenue and expenditure of the Consolidated Fund Services (CFS) and the Public Sector Pooled Pension Plan identified several items that could have been addressed in a different manner. The effect of these items on the Fund is measured as the additional revenue generated had these funds been invested in the PSPP Fund instead of being used as they were. These items are:

1. \$195 Million in unmatched employer contributions (1993-2014) – Government did not match employees’ contributions by up to \$20 Million annually
2. \$37 Million in Federal and Provincial pension related revenues paid to Consolidated Fund Services (CFS) (1981-2014)
3. \$58 Million in NL Hospital Association Pension unaccounted for (1984)
4. \$75 Million for retiring employees under the Roads for Rails Program (1988)
5. \$101 Million in Deficiency Payments to Uniformed Services and MHA pension plans (1981-2014)
6. \$230 Million in Ex-gratia payments (pensions paid to individuals who did not make any contributions to a pension plan) from Consolidated Fund Services. The value of Ex-gratia payments made from the PSPP Fund was not available for analysis.

Potential Value Added

Decision	Cost	Added Value
1. Unmatched Employee Contributions	\$195 M	\$432 Million
2. Federal & Provincial Revenues	\$37 M	\$157 Million
3. NL Hospital Association	\$58 M	\$732 Million
4. Roads for Rails	\$75 M	\$591 Million
5. Deficiency Payments	\$101 M	\$429 Million
6. Ex-gratia (CFS) Payments	\$230 M	\$703 Million
7. 1981 Unfunded Liabilities Paid	\$489 M	\$9,474 Million
TOTAL	\$1,185 Million	\$12,518 Million

The PSPP Fund would have had an extra \$12.5 Billion in assets in 2014 had Government managed it differently.

Beneficiaries are less informed about the management of their PSPP Fund than they could be. A large amount of information about the operation and management of the PSPP Fund exists and is collected and monitored by Government. Substantially less information is shared with the beneficiaries of the Fund. Multiple reporting agencies, large-scale data aggregation, different reporting periods, unclear categories such as Ex-gratia and Provincial Revenues, and a general lack of transparency have exacerbated the situation.

AN EXAMINATION OF THE PUBLIC SECTOR POOLED PENSION FUND

Introduction

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The PSPP Fund was established in 1980 to finance benefits under the Government sponsored pension plans. The Minister of Finance is the Trustee of the Fund. The Pension Investment Committee Investment Committee advises the Minister on the operation and investment of the Fund.

The liability associated with employee future benefits, which include pensions and group health and life insurance benefits, grew to \$6.5 Billion. (Auditor General, 2014) The most recent information about the Fund can be found in the 2013 Annual Report of the Pension Investment Committee.

An analysis of the past 34 years (1980-2014) of Reports of the Auditor General, Public Accounts, Financial Statements of the PSPP Fund and Annual Reports of the Pension Investment Committee resulted in the most detailed public database of Fund information. It includes: contributions; pensions; rates of return; investment income; balances; and participants.

Information from these reports and the database was used to describe the Public Sector Pooled Pension Fund, the unfunded liabilities and the effects of Government's decisions on both.

Pension Plans & Unfunded Liabilities

".... pensions are a form of compensation offered for services rendered and accrue over the years employees render those services." Public Sector Accounting and Auditing Committee (PSAAC), Canadian Institute of Chartered Accountants

Pensions are deferred wages. Employees and employers can choose between higher wages now or lower wages now and a pension when they retire.

When pensions are chosen, employees and employers agree on the details of the pension benefits, for example, how benefits will be earned, the amount of the pension and retirement eligibility.

Once the details of the pension are agreed upon actuaries calculate how much money is needed to fund the plan based on a number of factors including interest rates, salaries, expected lifespan, employee turnover and inflation. Employees and employers decide on how to share the cost of the plan, how the money will be invested and managed, and a pension plan is then started.

Under this model, as long as the actuarial calculations are correct, the money paid into the plan each year should equal the value of the pension benefit earned.¹ There should be no unfunded liabilities in the pension plan.

Unfunded liabilities occur when the value of pensions due employees is greater than the assets in the pension fund. Money owed is greater than the money in the fund plus the returns (interest) it will earn.

If the number of people receiving pensions from the plan increases, contributions to the plan must increase proportionally or there will be an unfunded liability. As money owed goes up, money paid into the Fund should too.

Lower interest rates than expected by the actuaries will lower the value of the plan. There will be less money in the bank to pay for the pensions.

Higher salaries, longer lifespans, and higher inflation than expected will increase the value of pensions owed. More money will be needed to pay for future pension benefits.

Accounting policy changes may also affect the value of a pension plan. For example, valuing pension benefits as they are earned instead of when they are paid out increases the value of liabilities even if there are no other alterations to the plan.

Changes in any factors that increase the value of pension benefits owed from the fund, or lower the value of contributions to it, can create an unfunded liability.

¹ This is a simplified description of pension plans but is sufficient for the following analysis. Specific details of contribution rates and benefits the PSPP Fund can be found in the Public Accounts.

Database

The NL Public Sector Pensioners' Association now owns the largest database of pension information available to the public. It is comprised of approximately 2,000 data points spanning 48 years (1967-2014). Data from 1967 to 1980 were collected during the study "Past Government Actions on the Present State of the Pooled Pension Fund". Data from 1981 to 2014 were collected during the preparation of the current report.

The database includes information on contributions, pensions paid, investment income, interest rates earned, assets, revenues, deficiency guarantees, special payments, administrative costs, ex-gratia payments, unfunded liabilities retirees and contributors.

Data have been gathered from Financial Statements of the Pooled Pension Fund, Pension Investment Committee Annual Reports, the Public Accounts – Volumes I to V and both the Auditor General's Reports on Departments and Agencies and Audit of the Financial Statements. Data from these sources are reported in single year increments in text format.

Combining these data into a single, longitudinal database that can be analyzed and used represents a powerful analytical tool and an enormous source of information. This database provides the basis for the findings of this report.

It is important to note that this does not represent all existing information about the PSPP Fund. Considerably more is contained with the Payroll Databases of the Department of Finance and the Pensions Division of the Provincial Government but is it not available to the public.

An archive of 318 documents, news articles, reports, letters, press releases and other material from the Legislative Library of the Provincial Government and the Center for Newfoundland Studies at Memorial University has also been created. It represents the largest collection of Public Sector pension related material held outside the Provincial Government. This reference material is catalogued and partially indexed within a program called Mendeley. It is a free online reference manager and PDF organizer. It is easy to use and manage and compatible with other similar-purpose software.

The database, reference documents and associated background materials will be maintained by the Newfoundland and Labrador Public Sector Pensioners' Association.

The Public Sector Pooled Pension Fund

The Public Sector Pooled Pension Fund is comprised of 5 pension plans. They are the pension plans of: the Public Service; Teachers; Uniformed Services; Members of the House of Assembly (MHAs); and Provincial Court Judges which was added in 2004.

Benefits and other pension specifications are described in the respective collective agreements governing each plan. Plans are cost-shared with Government, as the employer, matching employees' contributions to the fund.

The Fund is invested in a diversified portfolio of assets. A Pension Investment Committee is responsible for monitoring, managing and reporting on the activities of the PSPP Fund.

The PSPP Fund must generate an average annual rate of return of 6.75% on its investments to pay for the value of pensions earned during the year (Department of Finance, 2014). The Public Sector Pooled Pension Fund has achieved an average annual rate of 8.8%, more than enough to compensate employees for the pensions they earn each year. (Pension Investment Committee, 2013)

Additionally, contributions to the Public Service pension plan have been sufficient to pay for pension benefits earned by members since the beginning of the PSPP Fund. (Mercer, 2013) In 1991, after a rate change, contributions by Teachers and Uniformed Services employees also offset pension earned by those employees each year. The MHA plan continued to receive contributions that were less than the value of pensions earned by contributors for an undetermined time afterward. (Auditor General, 1997)

The PSPP Fund was established to provide for the pensions employees earn and pay for during their working career. Contributions to the Fund, both employer and employee, represent deferred wages of employees. The PSPP Fund is money owed to employees for hours worked and money contributed. The Fund is held in trust by the Minister of Finance on behalf of the beneficiaries of the respective pension plans.

The Pension Investment Committee and Minister of Finance, as Trustee, are currently responsible for the \$7.9 Billion in assets in the PSPP Fund.

Historical Contributions and Pensions

Almost \$5.9 Billion in regular employee and employer contributions were made to the Public Service Pooled Pension Fund between 1981 and 2013. If all of these contributions had been invested in the Fund's assets it would be worth about \$18.9 Billion now.²

Special Payments to the Fund total \$4.7 Billion more.³ If both special payments and regular contributions had been invested to earn the same interest as the pension plan, the Fund would be worth \$25.9 Billion.

A total of \$7.7 Billion has been paid out in pension benefits during that same time.

Contributions paid into the Fund approximately offset pensions earned by Public Service Pension Plan employees for all 32 years (1981-2013). (Mercer, 2013). These contributions represented about 67% of the total Fund assets until 1990.⁴ After 1990-91, contributions into the Teachers and Uniformed Services plans also offset pension benefits earned by their employees.

Since 1991, about 99% of all annual employee and employer contributions to the Public Sector Pooled Pension Fund were sufficient to pay for the pensions earned during the year by the employees' making the contributions.

In at least one year, 1998, contributions to most plans were greater than the value of benefits earned in the plans. (Auditor General, 1997) This is called a current service surplus and it increased the value of plans by:

- \$16.5 Million for the Public Service
- \$1.5 Million for Teachers plus \$8.6 Million in the Ancillary plan
- \$1.1 Million for Uniformed Services.

In that same year, MHAs paid \$737,561 less in contributions than they earned in pension benefits. This means not enough money was contributed to their plan to pay for the pensions they will receive when they retire.

² Annual contributions are invested at the historical rates of return of the PSPP Fund.

³ Sum of Special Payments to PSPP Fund as recorded in the PSPP Fund Financial Statements 1981-2013.

⁴ If all Public Service contributions offset pensions earned and 67% of all contributions to the Fund were into the Public Service plan, we can conclude that most contributions to the PSPP Fund before 1991 offset pensions earned during that time.

The vast majority of contributions to the plan were sufficient to pay for the pensions earned between 1981 and 2013.⁵ Under this premise, subtracting pension payments from contributions each year and investing the remainder to earn interest would result in Fund assets of about \$7.8 Billion and \$0 unfunded liability.⁶

The \$6.5 Billion Liability⁷

Table 1: Unfunded Liability of PSPP Fund by Source, 2013 & 2014 (\$Billions)

	2013	2014
Public Sector Pooled Pension Fund	\$3.178 B	\$3.779 B
Memorial University Pension Plan	\$0.092 B	\$0.129 B
Group Health and Life Insurance	\$2.323 B	\$2.554 B
TOTAL Unfunded Liability	\$5.593 B	\$6.462 B

Source: Public Accounts, Government of Newfoundland and Labrador

The unfunded liability associated with employee future benefits for employees of the Government of Newfoundland and Labrador was \$6.5 Billion in March 2014. That is an increase of \$0.9 Billion from the \$5.6 Billion reported in March 2013.

Employee future benefits and the unfunded liability can be divided into 3 components: Group Health and Life Insurance; Memorial University Pension Plan; and the Public Sector Pension Plan (PSPP) Fund.

Only \$3.8 Billion, or 58%, of the unfunded liability can be attributed to the PSPP Fund.

The Memorial University pension plan is not part of the PSPP Plan and its liability is calculated separately.

Group Health and Life Insurance Benefits are part of the collective agreements of Government employees. Benefits are extended to retirees as described in the agreements on a 50-50 cost shared basis. This is not associated with the PSPP Fund. Despite agreeing to provide these benefits during the collective bargaining process, Government has not made any provisions to

⁵ Annual contributions offset annual pensions earned in the Public Service plan, representing about 67% of all pension contributions from 1981-1990. After 1991, contributions offset pensions earned in all plans (except MHA's) or 99% of all pension contributions were sufficient to pay for the pensions earned by current employees.

⁶ Value of fund in year_i = (value in year_{i-1} * (1 + interest rate)) + (contributions + special payments – pensions in year_i)

⁷ The section has been updated to incorporate the Public Accounts for the Fiscal Year 2013-14 released October 29, 2014.

meet these obligations. Money has not been allocated to pay for the promised benefits. This lack of planning has created an unfunded liability of almost \$2.6 Billion.

The unfunded liabilities associated with Group Health and Life Insurance retirement benefits was first recorded in the Public Accounts in 2003. This is an example of an accounting change affecting the value of the fund. These liabilities always existed. In 2003, they were officially acknowledged as a debt of Government.

Table 2: Unfunded Liability of the PSPP Fund, 2013 & 2014 (\$Billions)

	2013	2014
Public Service	\$1.930 B	\$2.278 B
Teachers'	\$0.970 B	\$1.193 B
Uniformed Service	\$0.189 B	\$0.214 B
MHA's	\$0.077 B	\$0.081 B
Judges	\$0.012 B	\$0.015 B
TOTAL	\$3.178 B	\$3.779 B

Figures do not add to total due to rounding. Source: Public Accounts, Government of Newfoundland and Labrador

The unfunded liabilities associated with the different plans in the Fund are shown in Table 2.

Contributions to the Public Service Pension Plan have been sufficient (large enough) to pay for the pensions earned by contributors, since 1981, as shown in the last section. However, there is still \$2.3 Billion in unfunded liabilities in the plan.

Two-thirds (\$0.6 Billion) of the increase in total unfunded liabilities from 2013 to 2014, shown in Table 1, can be attributed to the PSPP Fund as shown in Table 2. Debt, like assets, grow with interest. Interest on the existing unfunded liability, at \$0.35 Billion in 2013 (Auditor General, 2014) is the main reason the PSPP Fund unfunded liabilities grew.

Historical Unfunded Liabilities

The Public Sector Pooled Pension Fund was established in 1980. Before the fund was created, employees contributed 5% of their salaries to the public service pension plan and were promised a pension in return.

Government collected employee contributions and deposited them into the Consolidated Revenue Fund, which is like a general bank account for Government. Government did not match the contributions, nor were employees' contributions invested to earn interest. In fact,

Government spent employees' pension contributions as they would have spent tax revenue, on the general operation of Government. Pension contributions were used to provide public services instead of saved for the pensions they were supposed to provide.

Pensions to retirees were paid out of the Consolidated Revenue Fund as they came due. This created a pay-as-you-go system.

The PSPP Fund ensured employees' contributions were matched by the employer and contributions were invested to pay pension benefits in the future.

Employees contributing to Government pension plans before the Fund was established were credited with pension benefits under the Fund. However, Government did not deposit employees' contributions from before 1981 (that money had already been spent) nor make a matching employer's contribution nor was any interest earned pre-1981 to provide for these benefits.

This means that when the Fund was created there was a deficit. Government already owed more in pensions than there was money available on deposit in the Fund. An actuarial valuation done in 1977 identified \$489 Million in unfunded pension liabilities. (Auditor General, 1982)

These actions created a situation where pension benefits earned before the Fund was established were being paid out of new contributions to the Fund. After 1981, employees who thought they were saving for their own retirements were actually making up for the pensions earned by employees and the contributions made, but not saved by Government, before 1980.

In doing so, less money remains to be invested and grow to provide a pension for employees in the PSPP Fund. Less money invested means fewer assets in the plan and the unfunded liability grows.

Another actuarial study was completed in 1984. The unfunded liabilities in the plans for 1977 and 1984 are given in Table 3.

Table 3: Unfunded Liabilities PSPP Fund 1977 & 1984

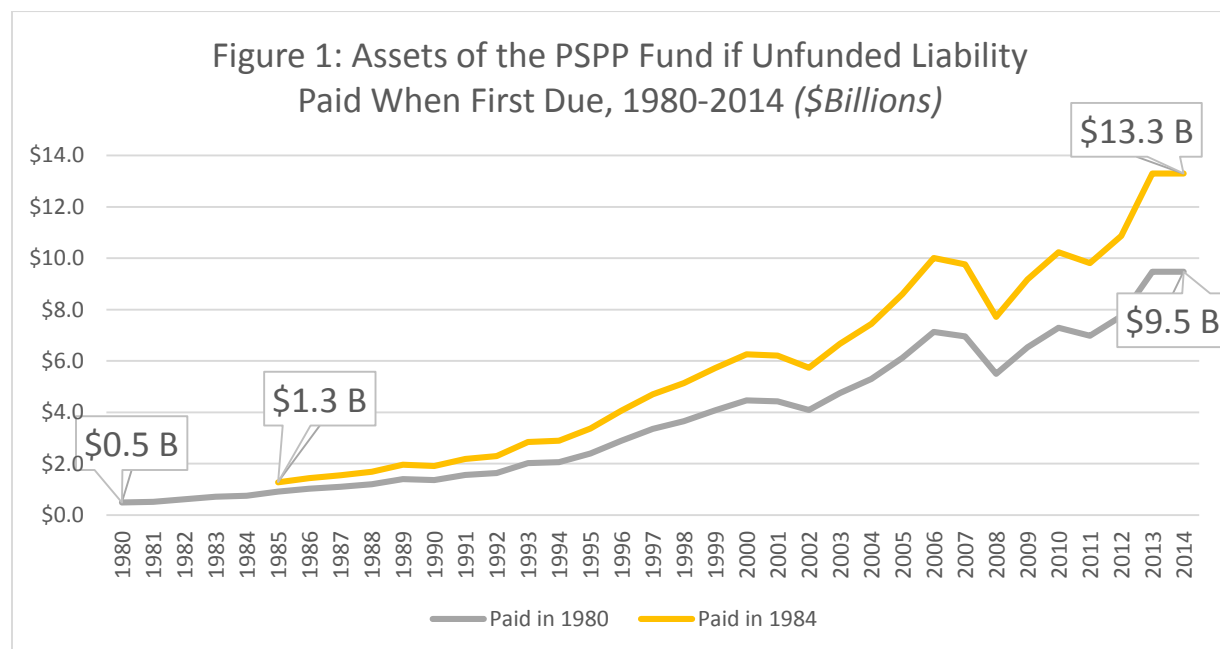
	1977	1984
Public Service	\$217.3 Million	\$509.7 Million
Teachers'	\$229.6 Million	\$674.5 Million
Unformed Services	\$37.0 Million	\$85.8 Million
MHA's	\$4.9 Million	\$11.8 Million
TOTAL	\$488.9 Million	\$1,281.8 Million

Source: Public Accounts, Government of Newfoundland and Labrador

Figure 1 shows the value of PSPP Fund assets if Government had chosen to address the unfunded liabilities of the PSPP Fund when the Fund was established. The full amount of the 1977 and 1984 unfunded liabilities are assumed to be paid into the PSPP Fund in 1980 or 1984 respectively, and earn the same rate of interest as the Fund did between 1981 and 2013⁸.

Had Government paid \$489 Million into the PSPP Fund in 1980 there would be an additional \$9.5 Billion in the fund in 2014. If, instead, Government waited until 1984 and paid \$1.28 Billion into the Fund to cover the unfunded liabilities at the time, there would be an additional \$13.3 Billion in assets in the Fund.

The \$13.3 Billion in assets in the PSPP Fund is substantially higher than the unfunded liability associated with the PSPP Fund of \$3.8 Billion and the total unfunded liability of \$6.5 Billion.



Source: Author's calculations.

⁸ Using the historical rates of return on investments of the PSPP Fund.

Effect of the Pension Holiday

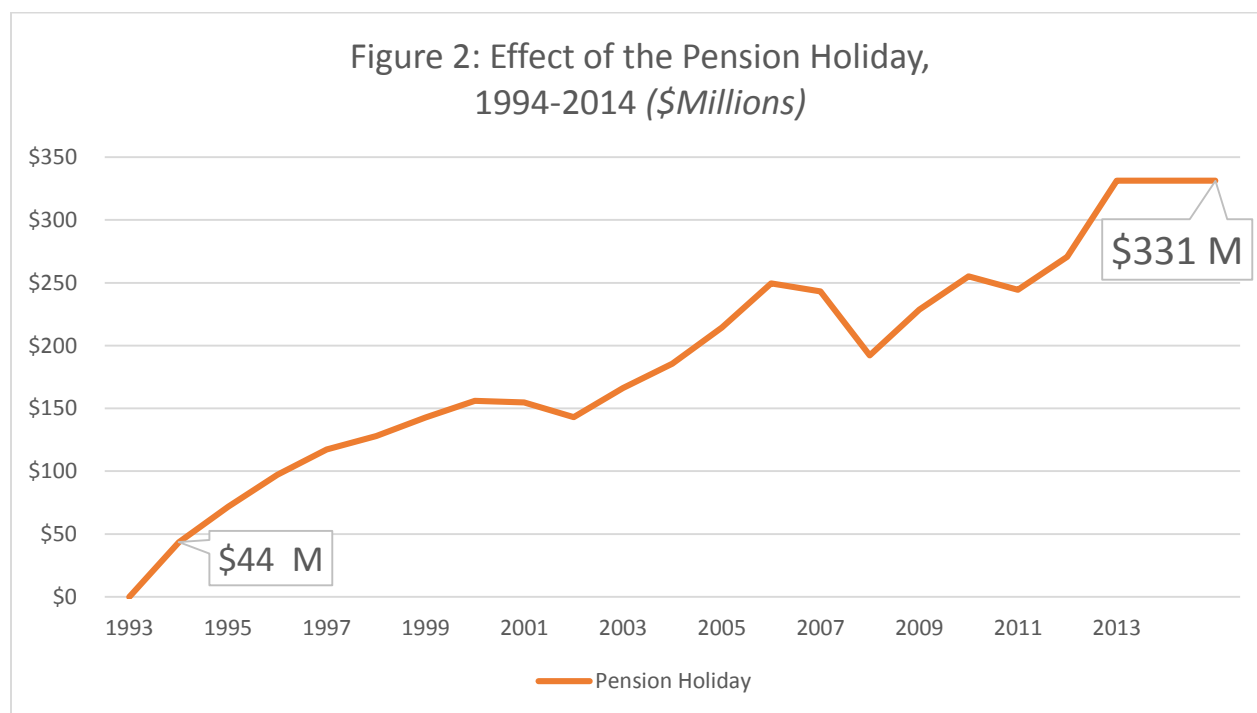
Between 1993 and 1996, Government chose to reduce Government employer's contributions to the Public Service Pension Plan. Pension benefits were also reduced in this time period. Consulting actuarial studies indicate this did not significantly affect the funded position of the Fund. (Auditor General, 1997 & Mercer, 2013) There was a zero net effect on the plans assets.

If Government had reduced benefits but maintained employer contributions between 1993 and 1996, total contributions to the Fund would have been higher by \$74 Million:

- \$43 Million in 1993;
- \$18 Million in 1994;
- \$9 Million in 1995; and
- \$4 Million in 1996.

There would be \$331 Million more in the Fund in 2014 if this \$74 Million over 4 years had actually been contributed and earned interest in the PSPP Fund, as shown in Figure 2.

In 1994, when Government reduced employer contributions to the Public Service plan by \$18 Million, an extra \$22 Million in employer contributions were made to the Teachers' Pension Plan.



Source: Author's calculations.

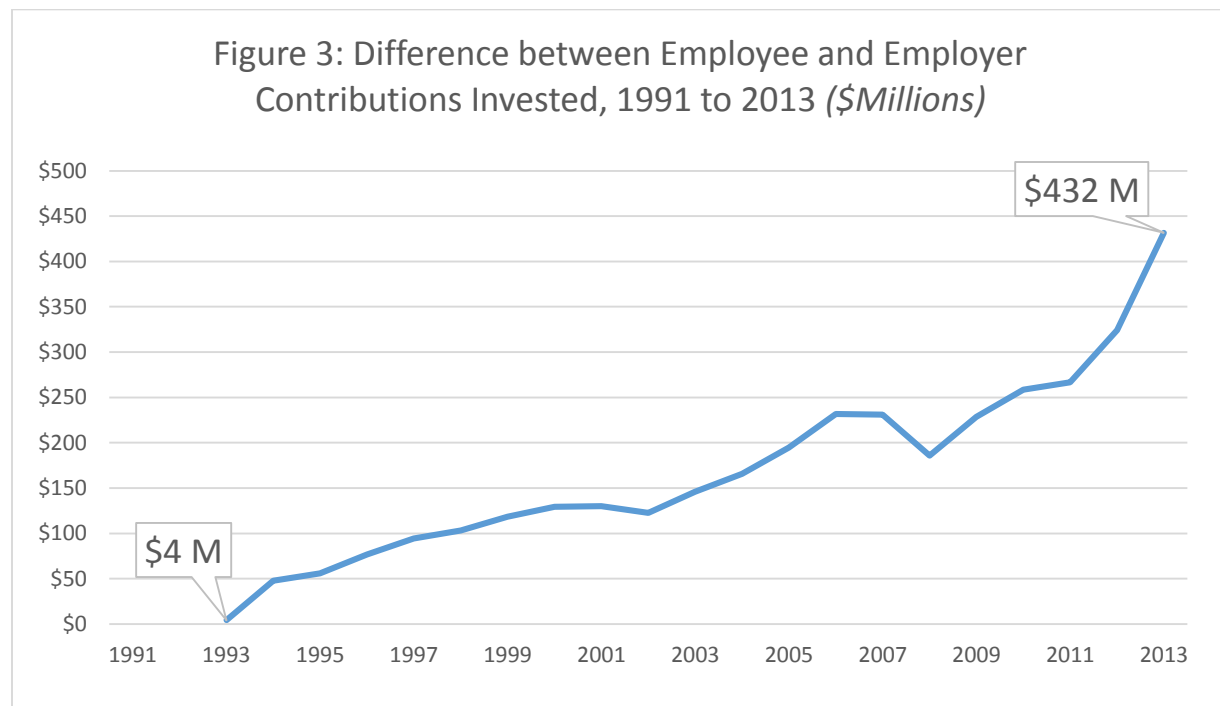
Matching Employees' Contributions

The Province is required by law to match employees' contributions for current service. Matching may also occur for other types of prior service purchased under contract. (Pension Investment Committee, 2013)

In 1991, the Financial Statements of the PSPP Fund began reporting employee and employer contributions.⁹

Between the pension holiday and 2009, employer contributions were less than that of employees by up to \$6.3 Million each year. The gap between employer and employee contributions has increased to more than \$20 Million per year in each of 2010, 2011, 2012 and 2013. Government has paid \$80 Million less into the pension fund than employees in the past 4 years.

If Government had matched all employee contributions to the PSPP Fund there would be \$432 Million more in the Fund.



Source: Author's calculations.

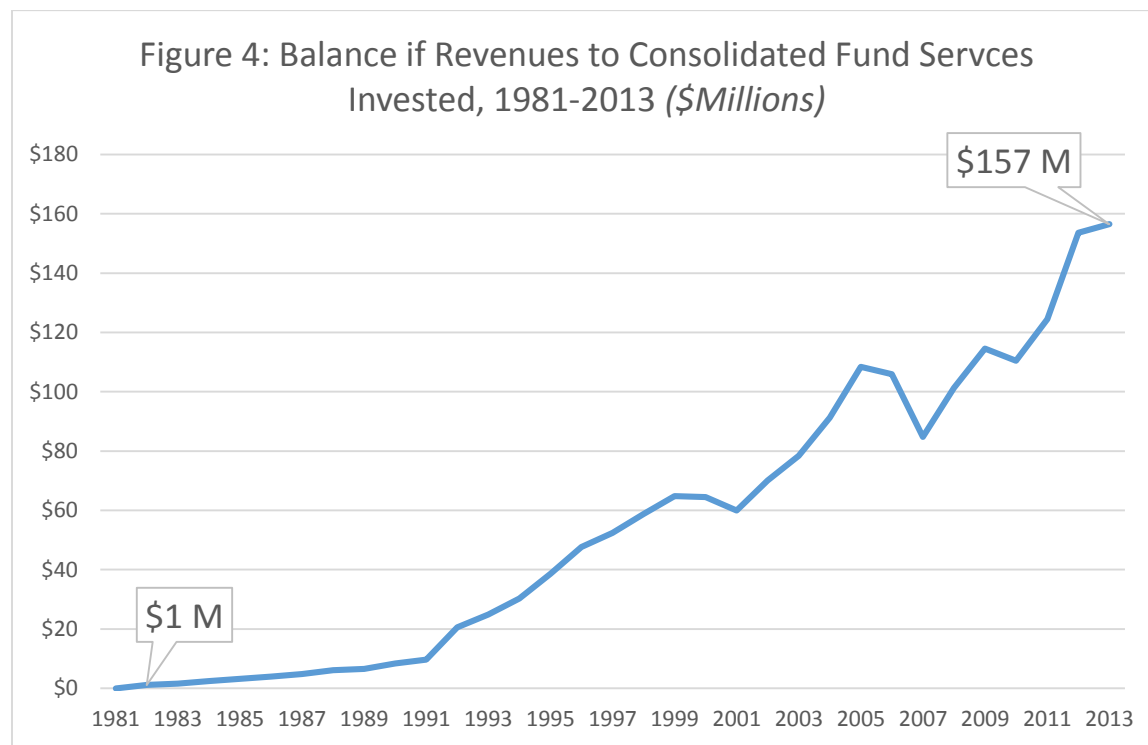
⁹ Prior to 1991, only total contributions were reported. (Financial Statements, Pooled Pension Fund, 1981-2013)

Federal and Provincial Revenues & Pensions

Consolidated Fund Services (Government's bank account for pensions)¹⁰ records money received from Federal and Provincial sources designated for pensions. These revenues are categorized as either Contributions to Pension Fund, Ex-gratia Payments or Special Acts. No description of the nature of these payments or why they are being made is provided in the Public Accounts.

\$36.6 Million in pension related revenues were received by Consolidated Fund Services between 1981 and 2013.

Investing all these revenues in the PSPP Fund as they were received would have increased the Fund's assets by almost \$157 Million.



Source: Author's calculations.

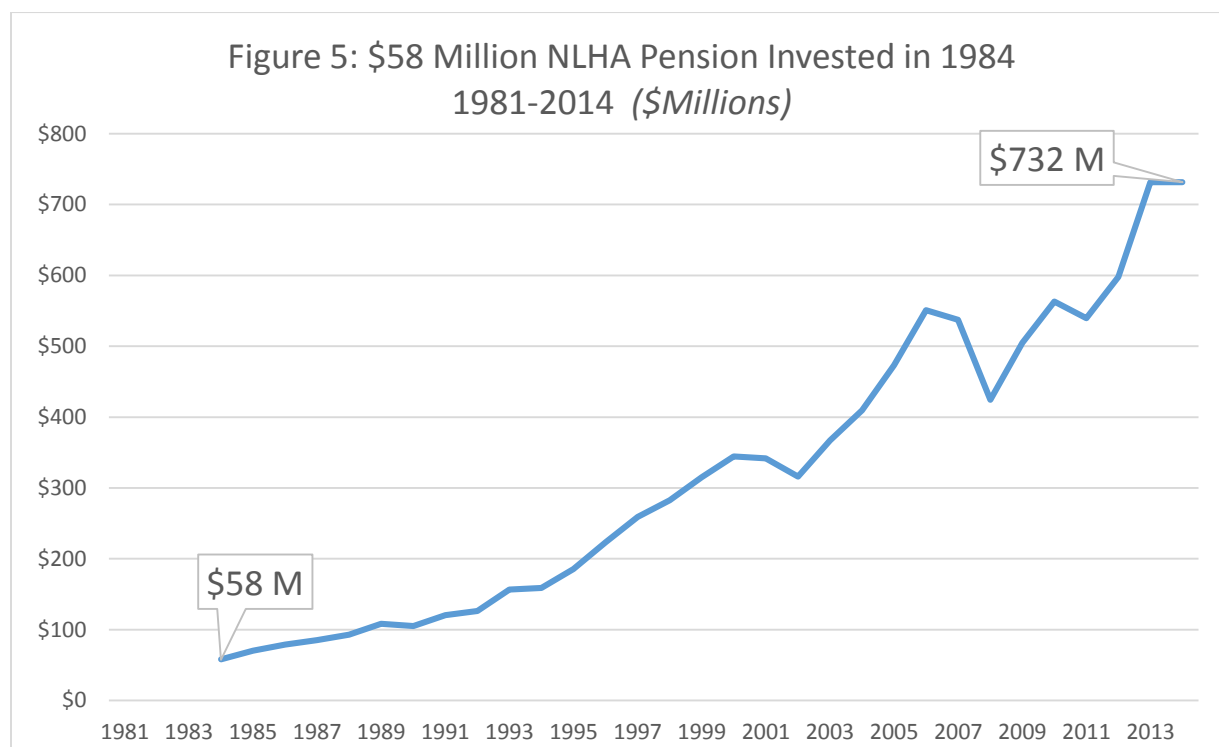
¹⁰ Expenditures from Consolidated Fund Services are made to fund pension plans for Government and its agency employees.

NL Hospital Association (Janeway) Pension

In 1984, the responsibility to provide pension benefits to employees of the Janeway hospital was transferred into the PSPP Fund.¹¹ Prior to that, these employees had saved \$58 Million in a pension account with Royal Trust. There is no record of the \$58 Million pension surplus belonging to these employees being transferred into the PSPP Fund.

If Government did add these employees and the value of their earned pensions to the PSPP Fund but placed the \$58 Million elsewhere, it increased the pension benefits to be paid out of the PSPP fund without increasing the Fund's assets. This action would effectively increase the unfunded liability of the PSPP Fund.

Had the \$58 Million pension surplus been invested in the PSPP Fund in 1984, there would be an additional \$732 Million in the Fund in 2014.



Source: Author's calculations.

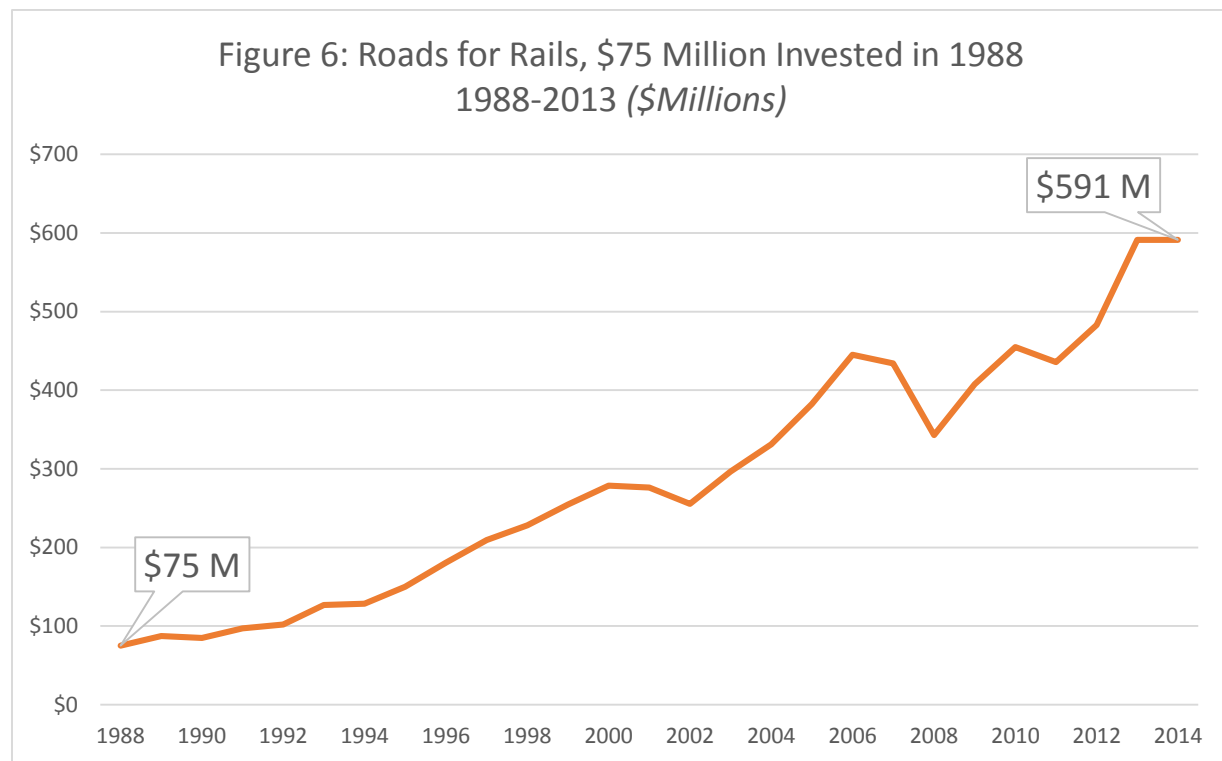
¹¹ Accounts of employees affected and other stakeholders. Existing evidence and an appeal to Government have failed to clarify how the money and employees were allocated.

Roads for Rails: Canada Newfoundland Transportation Initiative

The closure of the Newfoundland Railway resulted in an agreement with the Federal Government where Newfoundland and Labrador would receive a lump-sum payment for roads and infrastructure improvements and pensions for former Canadian National Railway employees.

\$75 Million of the \$800 Million agreement was earmarked for this labour force adjustment. (MOU, 1988) Records indicate the \$75 Million was not transferred into the PSPP Fund.

Had this \$75 Million been invested in the PSPP Fund in 1988, when the agreement was finalized, there would be \$591 Million more in the Fund in 2014.



Source: Author's calculations.

Government Money Purchase Plan (GMPP)

When employees transfer from the Government Money Purchase Plan (GMPP) to the PSPP Fund, the value of their contributions, plus the employer's share are also transferred.

The interest earned on the employee and employer contributions while in GMPP is not transferred into the PSPP Fund.

The longer employees are in the GMPP, the more interest is left in the GMPP (which should instead fund their pensions from the PSPP Fund) and the greater the increase in the unfunded liability of the PSPP Fund.

Further research could be done to compare the value of pensionable time transferred between plans to the value of assets transferred (i.e., were assets transferred sufficient to pay for the value of the pension transferred). Data likely exist in the Pensions Division Payroll Database to complete this analysis.

Provincial Court Judges' Pension Plan

The Provincial Court Judges Pension Plan was added to the Public Sector Pooled Pension Plan in 2004.

The Plan had \$1.2 Million in Assets in 2004 and an unfunded liability of \$3 Million.

Employees' contributions were slightly higher than employer contributions between 2004 and 2013. In 2009, the plan received a special payment of \$0.181 Million.

Plan assets were \$6.1 Million in 2013 and unfunded liabilities had grown to \$12.2 Million.

Members of the House of Assembly Pension Plan

Contributions to the Members of the House of Assembly Pension Plan have been less than the value of pension benefits earned (Auditor General, 1997) until at least 1999 when contribution rates increased and benefits decreased. In research to date, there has been no indication that benefits earned were offset by contributions after that time.

Government made \$25 Million in extra payments to the MHA pension plan because the payments out of the plan were greater than the contributions to it every year between 1981 and 2002. These are called deficiency payments.

The MHA pension plan has \$76 Million in unfunded liabilities now, compared to \$4.9 Million in 1981.

Deficiency Payments

Deficiency payments are required when the value of pensions to be paid¹² from a fund in a year are greater than the amount of money in the fund. Government is required by law, under the Pensions Funding Act 1981 to pay for any plan deficiencies that may occur. (Auditor General, 1987)

The Uniformed Services and MHA pension plans were established in 1981 with \$0 assets. Current employees' annual contributions were used to pay the pensions of retirees each year until 2003. Contributions were less than the value of pensions to be paid and Government made up the difference with deficiency payments during this time.

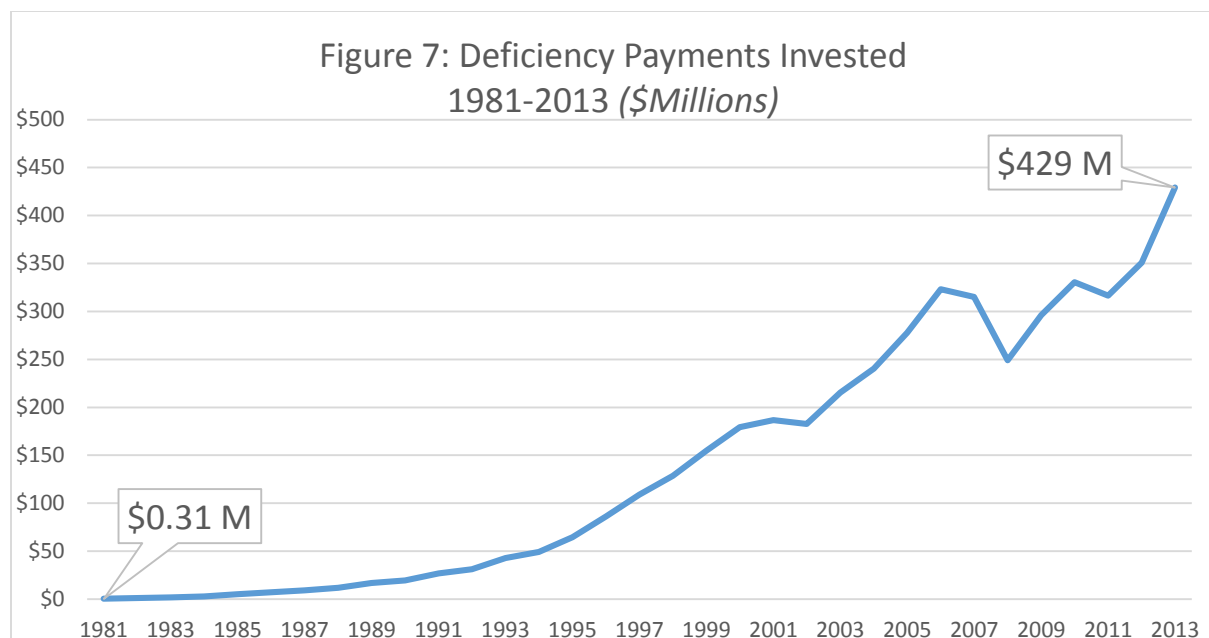
These deficiency payments totaled \$101 Million: \$76 Million to the Uniformed Service Plan and \$25 Million to the MHA's pension plan.

Consequently there was \$0 assets in both plans to invest and pay for the pensions of those actually making the contributions. This increased the unfunded liabilities in the plans.

The PSPP Fund would have an additional \$429 Million¹³ had the \$101 Million been invested instead of being used to make deficiencies payments. This is shown in Figure 7 below.

¹² Payments from a fund include pensions to retirees and refunds of contributions to employees withdrawing from a pension plan.

¹³ Assumes payments made in one fiscal year begin to earn interest in the next fiscal year at the same rate as the PSPP Fund.



Source: Author's calculations.

Accounting Policies

A number of accounting changes have been made since 1981. They include:

- Inclusion of unfunded liabilities in Statement of Expenditures and Revenues;
- Pension benefits accrue as they are earned; and
- Addition of Group Health and Life Insurance Liabilities.

These policies are generally in line with the standard accounting principles as prescribed by the Canadian Institute of Chartered Accountants. (Mercer, 2013)

Early Retirements and Severance

Severance payments are made from an employee's Department or Agency, not the PSPP Fund and therefore have no effect on the PSPP Fund.

Early retirements have no net effect on the Pooled Pension Fund. Service accumulation and pension contributions stop and pension payments begin based on rates outlined in the collective agreements when employees retire.

Plan Improvements

3 main improvements have been made to the PSPP Fund:

- Early retirement benefit added under Teachers' Plan;
- Modest indexing in 2000's; and,
- Early Retirement Incentive in 1990's.

These improvements had a net cost of \$200 Million (Mercer, 2013) or 3% of the total \$6.5 Billion unfunded liability.

Ex-gratia Payments

Government's ex-gratia payments are not clearly defined in any of the literature studied. Requests to Government for an official definition and how it is applied have not been met.

In general, ex-gratia payments are not required by law and are given "by favour." With respect to pensions, this seems to apply to pensions paid to individuals who did not make contributions to a pension plan.

Provincial ex-gratia payments appear to be recorded in 3 separate places: as payments from Consolidated Fund Services, and as both ex-gratia HARTT¹⁴ payments and other ex-gratia payments in the Public Sector Pooled Pension Fund.

Ex-gratia payments from the PSPP Fund have only been publically reported once (in 1997) in the history of the Fund's Financial Statements, Annual Reports of the Pension Investment Committee, or Auditor General's Reports.

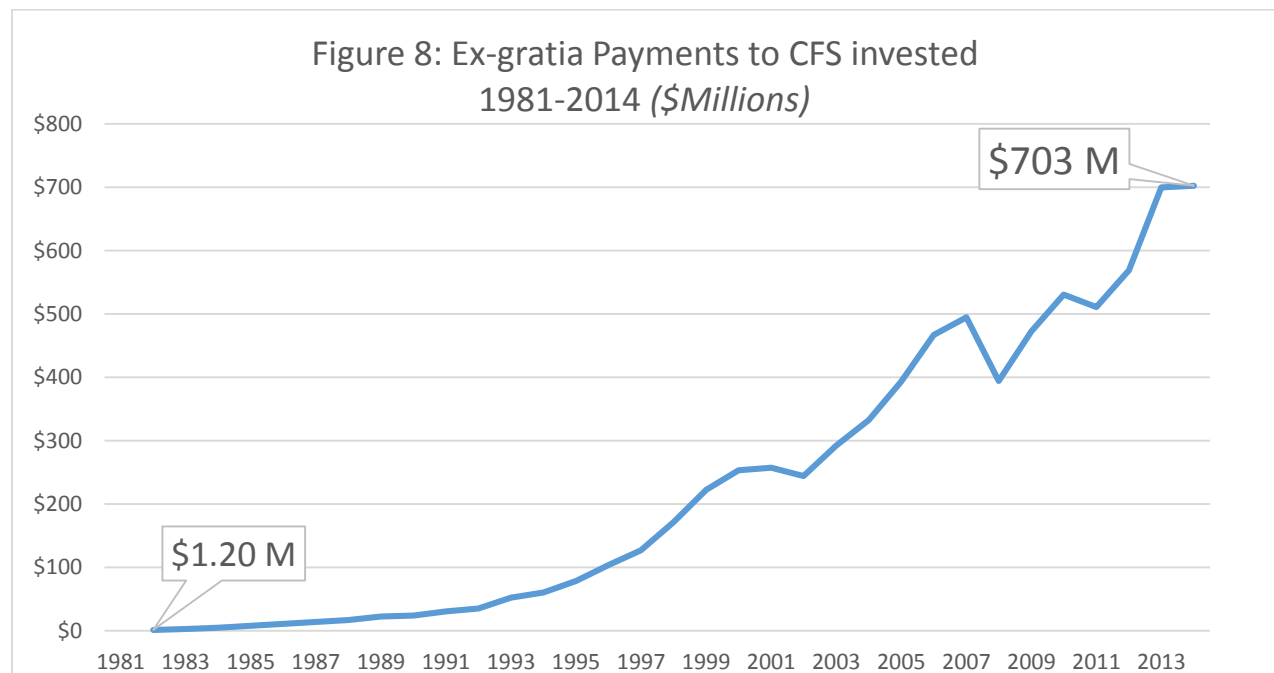
Ex-gratia payments from Consolidated Fund Services seem to be separate from the PSPP Fund. These payments are recorded in the Public Accounts.

\$230 Million in ex-gratia payments¹⁵ were made from Consolidated Fund Services between 1981 and 2013. Hansard indicates this may include payments to the Northern Cod Early Retirement Program. Other potential groups may include Abitibi workers from Grand Falls, Baie Verte Miners, Gander Airport employees, some Memorial University employees, as well as those of the Newfoundland Broadcasting Corporation.

¹⁴ Ex-gratia pensions granted to employees and widowers of the Waterford Hospital.

¹⁵ Ex-gratia payments become "Ex-gratia and Other Payments" in 1991. No clarification is given as to what is included in either.

There would be an extra \$703 Million in the PSPP Fund if these ex-gratia payments had instead been invested in the Fund. This is illustrated in Figure 8.



Source: Author's calculations.

Conclusion & Observations

The PSPP Fund represents the deferred wages of Public Sector Employees. Government has been entrusted to manage \$7.9 Billion in employee assets. The unfunded liability associated with this fund has grown from \$488 Million to \$3.8 Billion since the Fund's inception.

Interest on the debt represent 69% of unfunded liabilities.

"Funding the interest on the deficit was recommended as early as the 1960 Royal Commission report, but has never occurred." Mercer, 2013

Reports of the Auditor General substantiate the findings of the Mercer report.

Government has been aware of the unfunded liabilities of the Public Sector Pooled Pension Fund since before the Fund was started. Its knowledge of the problem extends to:

- the contributing causes;
- the size of the problem;
- rate of growth;
- problems arising as a result of continuing unfunded liabilities; and
- potential solutions.

Considerably more information is publically available about the revenue of the fund as compared to the expenditures. Administrative expenses are about 4% of all payments from the Fund. A description of them by type of expenditure and how costs are calculated across pension plans is provided. In comparison, pension payments are 96% of all Fund expenditures but only the total amount of pensions paid out in millions of dollars and the total number of pensioners in thousands is reported.

Beneficiaries are less informed about the management of their PSPP Fund than they could be. A large amount of information about the operation and management of the PSPP Fund exists and is collected and monitored by Government. Substantially less information is shared with the beneficiaries of the Fund. Multiple reporting agencies, large-scale data aggregation, different reporting periods, unclear categories such as Ex-gratia and Provincial Revenues, and a general lack of transparency have exacerbated the situation.

The Financial Statements of the Public Sector Pooled Pension Fund would be significantly different if the options considered within this report had been implemented. A summary of the results are shown in Table 4.

Table 4: Summary of Analysis

Decision	Added Value
Unfunded Liabilities paid in 1981	\$9,474 Million
Unmatched Employee Contributions	\$432 Million
Federal & Provincial Revenues	\$157 Million
NL Hospital Association	\$732 Million
Roads for Rails	\$591 Million
Deficiency Payments	\$429 Million
Ex-gratia Payments	\$703 Million
TOTAL	\$12,518 Million

Source: Author's calculations.

The Public Sector Pooled Pension Fund would have an extra \$12.5 Billion had Government chosen to manage the Fund differently.

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