Top 10 Funding Q&As

1 **Q: WHAT IS THE PENSION PLAN'S FUNDING STATUS?**

A: Despite double-digit investment returns for two consecutive years, the Ontario Teachers' Pension Plan reported a preliminary $17.2 billion funding shortfall as of Jan. 1, 2011. At that date, the plan had about 89% of the estimated funds required to meet its future pension obligations.

2 **Q: WHY DOES THE PLAN HAVE A SHORTFALL WHEN IT MADE LOTS OF MONEY LAST YEAR?**

A: The cost of future pensions is growing faster than plan assets, despite strong investment returns in 2009 and 2010.

Low real (after inflation) interest rates and long periods of retirements are two key reasons for this.

Long-term real interest rates are used to estimate the cost of future pensions. When interest rates fall, as they have in recent years, pension costs rise because more money needs to be set aside to earn the value of pensions that will be paid in the future.

Real interest rates declined to 1.1% at the end of 2010 from 1.5% at the start of the year.

Longer retirements and longer life expectancy are also factors. A typical teacher retiring today is expected to collect a pension for 30 years, four years longer than the average teaching career. In addition, a survivor benefit may be paid after the teacher dies.

These and other factors continue to make pensions more expensive than in the past.

In addition, the pension fund's 2008 investment loss will continue to be absorbed until 2012 due to smoothing. Smoothing is a technique commonly used in the pension industry to even out (or smooth) annual investment gains or losses to reduce volatility.

3 **Q: HOW WILL THE SHORTFALL BE RESOLVED?**

A: To address a funding shortfall, the Ontario Teachers' Federation (OTF) and the Ontario government, which jointly sponsor the Teachers' pension plan, could:

- increase contribution rates; or
- invoke conditional inflation protection for pension credit earned after 2009; or
- reduce pension benefits members will earn in future years; or
- adopt a combination of these options.

4 **Q: ARE MY PENSION BENEFITS GOING TO CHANGE?**

A: It's too soon to tell. The parties involved in sponsoring and administering the Teachers' pension plan recognize change will be required to address persistent funding shortfalls.

OTF and the Ontario government are required to address the current funding shortfall no later than 2012. They are considering all of the options outlined earlier. Members will be informed of their decisions as soon as they are reached.

5 **Q: IS MY PENSION SAFE?**

A: Current Ontario legislation protects the value of pension benefits already earned by working and retired members. Only contribution rates and pension benefits to be earned in future years can be adjusted during a teacher's career in response to funding shortfalls.

6 **Q: SHOULD I CHANGE MY RETIREMENT PLANS BECAUSE OF THE SHORTFALL?**

A: It's unnecessary to delay or advance retirement plans because of the shortfall or concerns about possible future benefit changes. Teachers' pensions are defined by a formula based on years of pension credit and average earnings. Basic pensions do not depend on the size of the pension fund or the funding status of the plan when you retire.

Top 10 Funding Q&As – continued

7 **Q: IS THE PENSION PLAN RUNNING OUT OF MONEY?**

A: No, the pension plan has $107.5 billion, enough to pay pensions for many years. But pension plans like the Teachers' plan are required to have enough funds to meet future pension obligations to all current members when looking ahead 70 years or more.

8 **Q: WHY DOES THE PENSION PLAN HAVE RECURRING FUNDING SHORTFALLS?**

A: Pension costs have been growing faster than plan assets for several years. When a shortfall arises, the plan has difficulty absorbing it because of the low ratio of working teachers to pensioners. There are only 1.5 working teachers for every retiree. As a result, a declining proportion of the plan's membership carries increased responsibility for meeting the plan's funding requirements.

Plan maturity - the low teacher-to-pensioner ratio - puts increased pressure on the pension plan to generate higher returns. But higher returns are difficult to achieve because the pension plan has a low risk tolerance due to its maturity. It must insulate itself from potential loss because of the low ratio of working to retired teachers and the desire for stable contribution rates. Since the plan has to take less risk, future long-term investment returns are projected to be modest.

9 **Q: HOW DOES THE PENSION PLAN DETERMINE WHETHER IT HAS ENOUGH MONEY?**

A: The pension plan board hires an independent actuary to conduct an annual funding valuation. The valuation determines the plan's financial health by comparing plan assets (such as stocks and bonds, as well as future contributions) to liabilities (the projected cost of future pensions).

The valuation shows whether there's a surplus of funds, a shortfall of funds or the right amount of funds to cover the projected cost of future pensions. Each valuation looks ahead more than 70 years to determine the pension plan's ability to pay benefits to all current members and their survivors.

To determine how much money is required to pay pensions, the actuary makes assumptions about the future inflation rate, future returns on invested assets, future salary increases, age at retirement, life expectancy and other factors.

10 **Q: WHO IS RESPONSIBLE FOR ENSURING THE PLAN CAN PAY PENSIONS?**

A: OTF and the Ontario government are responsible for ensuring the Teachers' plan is fully funded. OTF represents plan members and the Ontario government represents employers, such as school boards. OTF and the Ontario government negotiate the use of surplus funds and, when there is a funding shortfall, they decide how to resolve it. Surplus funds and the responsibility for absorbing shortfalls are shared equally by members and the Ontario government/designated employers.

OTF Your Voice. Your Strength. Ontario Teachers' Federation

Ontario

TEACHERS' PENSION PLAN ONTARIO

aefo Association des enseignantes et des enseignants franco-ontariens

ONTARIO ENGLISH Catholic Teachers ASSOCIATION

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