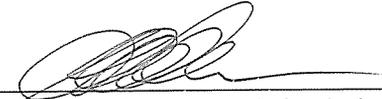


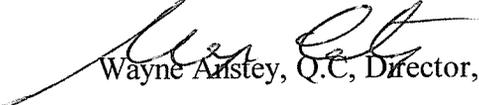
Halifax Regional Council
December 17, 2002

TO: Mayor Kelly and Members of Halifax Regional Council

SUBMITTED BY:


George McLellan, Chief Administrative Officer


S. Dale MacLennan, C.A., Director, Financial Services


Wayne Anstey, Q.C., Director, Legal Services

DATE: December 12, 2002

SUBJECT:

1. Increase in Current Service Pension Costs
2. Request for Changes to Solvency Rules Under Pension Benefits Act
3. Amendment to HRM Pension Plan Benefits

ORIGIN

Halifax Regional Municipality Pension Committee and advice from the Plan's Consultants.

RECOMMENDATION

IT IS RECOMMENDED THAT:

1. The employer portion of pension plan contributions be increased by .45% from 6.3% to 6.75% effective July 1, 2003.
2. The Province of Nova Scotia be requested to amend the Pension Benefits Act of Nova Scotia by:
"deleting subsections 79(1),(2),(3) ,(4) and (9); and amend or adjust any internal references in the Pension Benefits Act and Regulations thereunder to reflect these deletions"
And

that the Mayor send a letter to the Union of Nova Scotia Municipalities requesting support for this amendment.

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3. That the amendment being proposed by the HRM Pension Committee to change the termination benefit under the Halifax Regional Municipality Pension Plan (Plan) be approved in principle (see Attachment A).

BACKGROUND

The latest Actuarial Report on the Plan as at December 31, 2001 has resulted in a recommendation from the Plan's actuaries that to fund the accrual of existing benefits under the plan, there is a requirement to increase contributions to the plan by .90% of pensionable earnings.

In addition to annual actuarial valuations, the Pension Committee directed the Plan's actuaries to estimate the plan's financial results at August 31, 2002. As of this date, it was estimated that the plan's financial position had deteriorated considerably due to poor investment results.

The Pension Benefits Act of Nova Scotia requires actuarial valuations on two bases; a going concern basis and a solvency basis. The two bases are different; the solvency basis being determined on more conservative actuarial assumptions. In addition, remedies for deficiencies also differ, with solvency again, being the most conservative.

DISCUSSION

1. Increase In Current Service Costs

The current pension plan design was completed and approved based upon actuarial assumptions with an official implementation on April 1, 1998. The purpose of actuarial valuations is to periodically determine the plan's financial position based on actual Plan experience. Factors which may cause experience to be different than expected include the number of members taking early retirement, the increase in wage and salary rates, and most notably, the Plan's investment performance.

The Plan's Actuary has determined that the "Current Service Cost" of the plan has increased. This term refers to the contributions, based upon pensionable income, that must be made to the plan to fund the cost of the current benefits that are accruing to plan members.

Increases in Plan contributions are dealt with at Section 4.03 of the Plan as follows:

"4.03 Increase in Contributions

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If, on the advice of the Actuary, the contributions described in Section 4.01(1) are not sufficient to provide the minimum funding, as required by the Pension Benefits Act, of the benefits accruing in the Plan Year and any unfunded actuarial liability or solvency deficiency that may exist, then the Municipality's and the Members' Required Contributions shall be increased in equal amounts (expressed as a percentage of Member Earnings) so that the contributions are sufficient to provide the minimum funding required, subject to acceptability under the Income Tax Act. Should this arrangement not be acceptable under the Income Tax Act, in no event shall Member's contributions under the Plan exceed the normal cost of the Plan."

Since April 1, 1998, contributions to the Plan have been made at the rate of 12.6%, being split evenly between the employer and Plan members. The latest actuarial valuation as at December 31, 2001 indicates that current service costs expressed as a percentage of member's pensionable earnings is 13.5%, an increase of .90%. The increase required would be funded equally by the member and the HRM (or another participating employer, as the case may be). Therefore, members' and HRM contributions would each increase by .45% from 6.3% to 6.75%.

2. Request for Changes to Solvency Rules under the Pension Benefits Act

In addition to revealing the current service cost of benefits, the actuarial valuation determines whether there is a surplus or deficiency in the plan. The *Pension Benefits Act* requires that the plan funding be done on a Going Concern Basis and a Solvency Basis. As previously stated, each method has different rules of determination as well as remedial action which must be taken.

The financial markets have not been kind to investors generally, and our Plan has not been immune to the negative returns being experienced in markets throughout the world. Accordingly, the actuarial valuation on a going concern basis as at December 31, 2001 disclosed deterioration in the financial position of the Plan from the year prior. When applying the solvency test, the deterioration is greater.

The solvency test is applied to determine whether the plan would be solvent if it were required to pay all benefits to members as of the date the test is performed. Any deficiencies identified must be amortized over 5 years whereas on going concern basis, the amortization can be over 15 years. The Province of Nova Scotia exempts itself from this test. It is staff's view that this exemption is based upon the fact that, as a government, the Province of Nova Scotia will continue to exist no matter what happens in the financial markets. It is staff's view that the same rationale should apply to municipalities.

Although solvency calculations are prudent, there are some rules required under the mandated solvency test that could be regarded as extreme and which, in staff's view, put undue pressure on plans such as HRM's. One such item is the requirement to assume that all members who

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have at least “55 points” (combination of age plus service) will stay until retirement at their earliest date. This provision is known as the “grow-in” rule.

The elimination of “grow-in” in the calculation of liabilities on a solvency basis will decrease the total solvency liabilities to bring it closer to the going concern liabilities. However, should financial markets continue as they are, in the long term, both the going concern and the solvency requirements will mean significant increases in contributions, a change in benefits, or a combination of the two.

Under provincial pension legislation, the Plan is required to file an actuarial valuation every three years. The last one filed was as at December 31, 2000. Therefore, the next mandatory filing will be as at December 31, 2003 and which will be filed during 2004. Any increased contribution required to adequately fund the Plan would be incurred in 2004 and subsequent years.

Notwithstanding that filings are not mandatory until 2004, with the current financial markets and the general outlook for the future, staff are of the opinion that the HRM be proactive, both by anticipating future contribution increases or benefit changes which might control plan costs. The following table clearly demonstrates the effect the financial markets have had on the Plan’s financial health.

A	B	C
Valuation /Extrapolation* Date	Solvency Surplus (Deficiency)	Going Concern Surplus (Deficiency)
December 31, 1999	\$44,223,000	\$ 59,227,000
December 31 , 2000	\$43,995,000	\$ 63, 862,000
December 31, 2001	(\$39,271,000)	\$ 66, 202,000
August 31, 2002 *	(\$129,844,000)	\$ 60,268,000

* estimate only

The determination of the Plan’s position on a solvency basis (Column B above) was made based on the market value of fund assets. To mitigate the need for even greater additional contributions at this time, the actuarial value of assets will be used. On this basis the solvency deficiency estimated as at August 31, 2002 drops to \$47,485,000.

Furthermore, the removal of “grow-in” in the solvency calculation will reduce the estimated solvency deficiency at August 31, 2002 by another \$74,000,000, creating a solvency surplus of \$26,515,000 and therefore will soften the immediate impact of the increase in costs should

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financial markets not return to pre 2000 levels and will give the Pension Committee and the HRM time to prepare through either further increases in contributions, a reduction in benefits, or a combination of the two.

Accordingly, the recommended Pension Benefits Act amendment would seek an exemption from this requirement.

3. Amendment to HRM Pension Plan Benefit

The HRM Pension Committee has carefully considered plan changes which would be needed to support stability of contributions for both the Municipality and Plan members.

To avoid an even greater increase in contribution rates (estimated to be more than 3% in each of the next 5 years), the Pension Committee has proposed to reduce the Plan's cost by changing the termination benefit as of December 31, 2002. This change will affect active members in the *Current* (new plan provisions which were introduced on April 1, 1998) division of the Pension Plan whose employment terminates before becoming eligible for a pension.

These changes will affect benefits payable to members who terminate employment *on and after* December 31, 2002 and *before* becoming eligible for an immediate pension. As well, the change affects the benefit payable should a member die before becoming eligible for an immediate pension. The changes do not affect benefits payable to any members who retire from their employment and who are eligible to receive an immediate pension. This change is expected to reduce the actuarial liability by \$10,500,000 on a going concern basis.

Attachment A provides more detail of the proposed plan amendment for which the Pension Committee is seeking Council's approval and which will be distributed to all members of the plan.

BUDGET IMPLICATIONS

Provision will be made in the 2003/04 Operating Budget assumptions to provide funding for the employer share of the increased cost of benefits. The operating budgets of future years will include any future direction which the Plan may wish to take and as approved by Regional Council.

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FINANCIAL MANAGEMENT POLICIES/BUSINESS PLAN

This report complies with the Municipality's Multi-Year Financial Strategy, the approved Operating, Capital and Reserve budgets, policies and procedures regarding withdrawals from and the utilization of Capital and Operating reserves, as well as any relevant legislation.

ALTERNATIVES

1. Under the existing Plan provisions the HRM must contribute its share of the Current Service costs. With respect to solvency and funding deficiencies, Halifax Regional Council must approve any increases.
2. Regional Council may not wish to approve a request to amend the Nova Scotia Pension Benefits Act to adjust the Solvency test for "grow in". This is not recommended.
3. It is recommended that Council approve the amendment to the Plan which has been proposed by the HRM Pension Committee.

ATTACHMENTS

Appendix "A" - Proposed Plan Amendment

Additional copies of this report, and information on its status, can be obtained by contacting the Office of the Municipal Clerk at 490-4210, or Fax 490-4208.

Report Prepared by: Reg H. Ridgley, CGA, Manager, Strategic Capital Project Support

490-6475

Appendix A

Proposed Changes to the Pension Plan

SUBJECT TO UNION AND MUNICIPALITY APPROVAL

As with most investment vehicles in Canada and elsewhere in the world, the HRM Pension Plan has experienced financial difficulties due to poor investment market performance. As a result, Plan members and employers are facing increased contributions. To improve the Plan's financial health and maintain contributions at a reasonable level, two changes are set to take place.

Contribution Increase

Effective July 1, 2003, the defined benefit contribution rate for all Plan members, as well as the Municipality, will increase by 0.45%.

For example, if your...

Current contribution is...	Your contribution as of July 1, 2003 will be...
\$100 per pay	About \$107 per pay

This increase is necessary to adequately fund pensions being earned by members of the Plan.

Change in Termination Benefit

To avoid an even greater increase in contribution rates (estimated to be more than 3% in each of the next 5 years), the Pension Committee has proposed to reduce the Plan's cost by changing the termination benefit as of December 31, 2002.

▪ **Who is affected**

This change will only affect active members in the *Current* (new plan provisions which were introduced on April 1, 1998) division of the Pension Plan whose employment terminates before becoming eligible for a pension.

You are considered to be in the *Current* division of the Pension Plan if:

- you joined the Plan since April 1, 1998, or
- you converted benefits from a prior plan to the Current Plan or commenced membership in the Current Plan as of April 1, 1998.

▪ **About the change**

	Currently	As of December 31, 2002
If the sum of your age and service at termination equals at least 55	To determine your earliest unreduced retirement date (for example, the date you reach the Rule of 80), the Plan takes into account the period after termination as if your employment continued.	The Plan will NOT take into account any period after termination.
If the sum of your age and service at termination does NOT equal at least 55	The deferred benefit is indexed for each year from your termination date to the date you begin receiving your pension.	The deferred benefit will NOT be indexed.

▪ **Examples**

Terminating member whose age and service are equal to at least 55

If you terminate at age 48, with 20 years of service and average earnings of \$36,000:

Currently	As of December 31, 2002
You would be eligible for a monthly pension of \$1,200 starting at age 54 .	You would be eligible for the same monthly pension of \$1,200, but starting at age 60 .

Terminating member whose age and service do NOT equal at least 55

If you terminate at age 40, with 10 years of service and average earnings of \$36,000:

Currently	As of December 31, 2002
You would be eligible for an estimated monthly pension of \$890 starting at age 60.	You would be eligible for a monthly pension of \$600 starting at age 60.

These changes will affect benefits payable to members who terminate employment *on and after* December 31, 2002 and *before* becoming eligible for an immediate pension. As well, the change affects the benefit payable should a member die before becoming eligible for an immediate pension. The changes do not affect benefits payable to any members who retire from their employment and who are eligible to receive an immediate pension.

How does this change compare to the termination benefits of the prior municipal plans?

In almost all cases, the revised benefit will still mean a termination benefit that is better than the benefit you would have received under any of the prior plans. The possible exception would be the termination benefit a younger member would receive under the prior Metropolitan Authority plan.

We want to assure you that even with this change, the HRM Pension Plan continues to be a very good plan. In addition, this change will improve the financial status of the Plan and help to keep contribution increases to a minimum. Should additional changes to the Plan or contributions become necessary, we will advise you as soon as possible. Also, where applicable, we will seek the approval of bargaining units before proceeding with any Plan change.

The *Pension Benefits Act* of Nova Scotia requires that members be given formal notice of the change to the termination benefit. This notice is attached.

Should you have any questions, please contact your Pension Committee representative.

DRAFT

Notice to Members

of the

Halifax Regional Municipality Pension Plan

(pursuant to subsection 32(1) of the Nova Scotia *Pension Benefits Act*)

Effective December 31, 2002, termination benefits under the Halifax Regional Municipality Pension Plan ("Plan") are changing. The changes have been approved by the Municipality and affected bargaining units.

On and after December 31, 2002, a Plan member who participates under Appendix A of the Plan (the 'Current Plan') and who terminates employment after completing at least 24 months of Continuous Service while a member of the Plan will be entitled to receive an unreduced deferred pension, commencing when the individual attains age 60.

Before this change, for members of the Current Plan whose combination of age and service at termination equaled at least 55, the earliest unreduced retirement date under the Plan was determined by including the period after termination as if employment had continued for purposes of eligibility for retirement. This meant that some individuals might reach the earliest unreduced retirement date earlier than would otherwise be the case. For members whose age plus service did not equal at least 55, the deferred unreduced pension was payable at the earliest unreduced retirement date without assuming continued employment, but the deferred benefit was subject to annual indexing at the rate of increase in the Average Industrial Wage for each year from termination to pension commencement.

These changes affect benefits payable to members who terminate employment on and after December 31, 2002 and before eligibility for an immediate pension. They do not affect benefits payable to members who retire from their employment and who are eligible to receive an immediate pension.

If you have questions about these changes to the Plan, please contact your Pension Committee representative. If you have comments about these changes, please contact either the Plan Administrator or the Nova Scotia Superintendent of Pensions, at the addresses below.

HRM Pension Committee
Halifax Regional Municipality
P.O. Box 1749
Halifax, NS B3J 3A5
902-490-6213

Ms. Nancy MacNeill Smith
Superintendent of Pensions
Department of Environment and Labour
Pension Regulation Division
P.O. Box 2531
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902-424-4444