October 27, 2017 MEPB Stakeholder Governance Session
Questions and Answers (Q&A) Morning Session 9:00 to 11:00 AM

Presentation Segment 1: 9:29 – 9:57 AM

1) What is the role of the Government of Alberta (GoA) to MEPP? Why was the employer contribution rate reduced from 21.85% to 17.20%? Why did the GoA take all the reduction? Why can't MEPP members share some of the reductions?

   The Board makes recommendations to the President of Treasury Board, Minister of Finance (the Minister) on the total contribution rate of the Plan. Treasury Board and Finance makes a recommendation to Cabinet on the contribution rate split between the employer (ER) and employee (EE). Cabinet makes the decision on MEPP ER and EE contribution rates, which is approved and set by an order in council.

   The GoA has power to pass laws, and it is an employer to MEPP members. As an employer, the GoA collaborates with Alberta Pensions Services Corporation (APS) to administer the MEPP on behalf of members. APS must comply with all applicable pension regulations and rules, and fulfill its administrative duties. For example, an employer will decide whether to allow part-time employees to contribute to the Plan.

2) MEPP is exempt from funding solvency deficiencies. Does the Board receive information about the Plan on a solvency basis?

   The Plan's Actuary, Aon Hewitt, calculates the Plan's solvency in the valuation results. Solvency valuation provides an arbitrary value of the Plan. It does not necessarily reflect the Plan's financial reality and it can be misleading. Solvency valuation is more appropriate for private sector pension plans; it does not provide much value to the public sector pension plans. MEPP completes a solvency valuation in accordance with the Public Sector Pension Plans Act (the PSPPA).

3) Ontario is to relax solvency rules for defined benefit pension plans. Will this have an impact on how MEPP operates?

   The PSPPA does not require funding based on the solvency valuation results. However, if Alberta were to adopt similar changes, the Plan is well positioned to comply with these changes.

4) What are the pension benefits to a spouse if a MEPP member passes away?

   If a member dies before his/her pension partner (spouse), his/her pension partner receives a pension based on 75 per cent of the member's pension on pre-1992 service, and 66 2/3 per cent of the member's pension on post-1991 service.

   Pension benefit education to members is the role of the Plan's administrator, APS. APS Member Services can be reached by telephone or email and the contact information is available on the MEPP website.

5) What type of risk mitigation strategies are in place to manage the Plan's fund? What will the Board do if the market crashes? Is there a risk mitigation strategy other than to increase pension contributions? Can the Board recommend design changes?

   Diversification is the main risk mitigation strategy for investment management. The Board is looking at the possibility of changing the Plan's asset mix to include more alternative assets such as real estate, infrastructure, and private debt.

The Board has limited levers in managing the Plan; the Board can make recommendations on plan design changes but ultimately the Minister enacts these changes. For example, the Board made recommendations to the previous Minister on how to make MEPP more sustainable (maximizing pension benefits at a reasonable cost) in response to the 2013/2014 public sector pension plan reform.

6) The Board made a recommendation to the Minister to reduce the total contribution rate from 34.65% to 30%. Why did the GoA take the full reduction? Why can't MEPP members share some of these reductions? Is there a decision making process followed?

   The Board makes recommendations to the President of Treasury Board, Minister of Finance (the Minister) on the total contribution rate of the Plan. Treasury Board makes a recommendation to Cabinet on the contribution rate split between the employer (ER) and employee (EE). Cabinet makes the decision on the ER and EE contribution rates, which is approved and set by an order in council.

   MEPP is a multi-employer pension plan and the GoA is a participating employer; it has to follow employer policies and procedures. The GoA rightfully may want to recoup some past loss costs, while still maintaining consistency in the members' contribution rates.

7) MEPP is a joint defined benefit pension plan. Shouldn't employers and employees be jointly responsible for both risks and benefits associated with the Plan? Shouldn't the reduction to the total contribution rate be shared equally between employers and employees?

   The decision making related to the total contribution rate split is outside of the Board's purview. The normal cost of the Plan (without previous year's loss payments) is approximately 25%, and employers and employees share the normal costs of the plan equally. The Plan's ER and EE contribution rate split is close to 50/50 of normal costs.

   4.65% was removed from the previous total contribution rate of 34.65% - this was a special payment from previous years losses, amortized over 15 years, and ended on December 31, 2016.

8) The Plan's financial report as at December 31, 2016 indicates a surplus. Who owns the surplus? Will the GoA take the surplus away from the Plan?

   Accounting valuations and actuarial valuations are different, based on different assumptions, methodologies, and standards. According to the accounting valuation, the Plan is 103 funded%; however, according to the actuarial valuation as at December 31, 2015, the Plan is 92.71% funded. Therefore, the Board does not consider that the Plan has a surplus. The Plan has a funding policy, which requires the fund to build a buffer (contingency) to help stabilize the Plan's contribution rates. Whenever the Plan achieves a surplus with a 20% margin, the Board will attempt to best set the contribution rates to address the maturing nature of the Plan and mitigate longevity risks.

9) The GoA was trying to pool the Plan's assets during the 2013/14 public sector pension reform. Will MEPP members' pension benefits be protected against these changes?

   The Board was not aware at any time that the GoA was trying to pool the public sector pension plans' assets together. To clarify, the GoA wanted to close the MEPP to new plan members and make some plan design changes. They were also looking at Plan Governance. The 2014 pension reform bills, Bill 9 and 10, were not passed. The Board is not aware of any future plans to close the Plan.

Acting in the best interest of the Plan, the Board continues evaluating and measuring the Plan's risks and makes recommendations to the Minister. For example, the Board is concerned with termination methodologies and the impact to the Plan. The Board has consulted with the Minister on termination payment calculations.

The Minister is the Plan's Trustee; the Minister must consult with the Board on any plan rule changes; however, the Board can only act in an advisory capacity when it comes to Plan rule or design changes.

10) What survivor benefits are available? What happens if a spouse dies? What happens if a MEPP member dies before retirement?

    Survivor benefits are available to a surviving pension partner in the event that a vested MEPP member passes away prior to commencing a pension. Depending on your elected pension options, you can receive either a one-time lump-sum payment, referred to as a Transfer of Pension Value, or a lifetime pension, referred to as a Lifetime Immediate Monthly Pension.

    If a MEPP member dies before retirement, the Plan will pay out 100% of the commuted value of his/her pension entitlement up-to-date.

    There are different pension options - a member can make a choice based on their own circumstances. The Board's mandate does not cover pension benefit education. MEPP members are encouraged to contact APS MEPP Member Services for more information.

11) Why did the Board recommend the total contribution rate reduction when the Plan still has a deficit according to its 2015 actuarial valuation report? Is the Plan sustainable for a long-term?

    The contribution requirements are determined by the ***normal*** *cost of the Plan (without previous losses). The Board makes adjustments to the total contribution rate for the normal cost, to ensure sufficient funding for the Plan. A special payment of 4.65% ended on December 31, 2016, which resulted in the reduction of total contribution rate from 34.65% to 30%.*

    The Board applies a margin for liabilities to the total contribution (past losses and normal service costs) to manage contribution rate fluctuation. To assist with intergenerational inequity, the Board does not want to keep the contribution rates high for the current membership.

Presentation Segment 2: 10:05 - 10:32 AM

1) Is sustainability still an issue for the Plan? What kind of strategic initiatives including investment strategies did the Board take to ensure the Plan's sustainability?

    The Board conducts an environmental scan of the pension landscape and evaluates the challenges and opportunities that the Plan may face or faces. The Board makes recommendations to the Minister on how to improve the Plan's long-term sustainability.

    For the Plan's investment strategies, the Board looks at cash flow data, asset mix risk scenario testing results and other financial analysis. The Board consults with the Board's independent Investment Consultant to help mitigate risks and monitor investment performance.

The Board also looks at the future value of the Plan's liabilities, assess, and update the MEPP Investment Policy and asset mix, following an annual Asset Liability Study (ALS). This step helps to ensure that the Plan has an optimal asset mix within the allowed risk parameters.

The Board completes an annual Investment Manager review (due diligence review) of AIMCo, receives AIMCo's MEPP performance reports on a quarterly basis and receives annual presentations on major asset classes from the managers, including: HR, Finance (audit reports), Compliance, Responsible Investing, Enterprise Risk Management, Risk Management Program and Cyber Security.

2) Will the GoA's deficits have an impact on the Plan? Has the Board put policies and procedures in place to deal with financial crisis?

   The Board focuses on the Plan's funding deficits but not the GoA's deficits. The Board conducts stress tests to assess the impact of falling interest rates to the Plan. However, if the GoA has large deficits, it might affect the GoA's ability to borrow money, which will consequently affect Alberta's credit score and AIMCo's ability to invest in the Fixed Income asset class.

3) What does a mature plan mean? What are the risks associated with a mature plan? Is there a risk mitigation strategy for a mature plan?

   As a pension plan becomes more mature, the plan will have more liabilities and higher risks of cash flow shortage. According to the Plan's Actuary, a mature plan means a plan reaches a steady state, maintaining a relatively consistent proportion of the assets versus liabilities. The ratio of active (those contributing to the Plan) and pensioners (those drawing funds) changes and moves towards more pensioners than active members.

   The Board established a robust Funding Policy (utilizing contributions, benefits and asset mix) and Investment Policy to help mitigate risks associated with the Plan's maturity.

4) What was the Plan's funded status before 2012? What had the Board done to improve the MEPP's funded status?

   The Plan's funded ratio was 88.05% in 2012 and 87.58% in 2009.

   The Board commenced an annual modified ALS in 2013. For this study, the Board determines the Plan's funding needs by studying the actuarial cash flow data, which is taken from actuarial valuation or extrapolation data. The annual ALS ensures that the most current information is incorporated into the process of setting the asset mix, and that Plan assets are structured in the most efficient way to meet Plan liabilities and liquidity needs. This helps to improve the Plan's funded status.

   The Board also conducts an experience study every 5 years and adjusts the Plan's demographic assumptions if required. The last experience study was completed in May 2016, using the 2015 actuarial report data. As the Plan becomes more mature and members live longer, the normal costs of the Plan is increasing. The Board is fully aware of this challenge and has been proactively monitoring and managing this risk through many tools.

5) What is the Board's succession plan for Board members?

   The Board currently has two vacancies, and three board directors' terms will expire December 31, 2017. The Board identified the gaps in the current board membership including the two vacancies and with the three potential additional vacancies to Alberta Treasury Board and Finance (ATBF), and participated in a recruitment committee for the two vacancies and the three upcoming expiring terms December 31.

   The positions were posted by the GoA and the process adhered to the Public Agencies guidelines and set process. The Committee put forward recommendations to the Minister on candidates. The Board wants to fill all vacancies by the end of 2017, but the timing of the new board member recruitment is at the discretion of the Minister and Cabinet.

   The Board is aware of the potential for almost a full turnover of its membership, if two of the three members are not reappointed, effective January 1, 2018. We have strengthened our new board member onboarding program, education paths, updated Board policies and ensured that the Board's current practices are codified. Board culture and expectations are clearly set in the Code of Conduct and Charter of Culture and Expectations. The Board also includes board governance education in the new board member onboarding program.

6) Does the Board consider the potential reduction of manager positions in the GoA being a risk for the Plan?

   The Board has established an Enterprise Risk Management (ERM) program, and identified key risks, risk owners, existing mitigation strategies, and gaps. The decrease of the Plan's membership was included in the risk register and framed as maturity of the Plan (the active member to pensioner ratio is close to 1:1).

7) Has the Board's investment strategy changed in response to the stock market changes? Are alternative investments facing higher risks?

   The Board is completing an annual ALS to assess and balance risk and return trade-off, and to maintain an optimal asset mix. Alternative investments have provided investors with better risk adjusted returns over the past 10-year investment period, e.g. equities generated 6-7%, bonds generated 2-3%, real estate and infrastructure generated approximately 6%.

   The Board is looking at the possibility of increasing asset allocation in alternative investments and reducing asset allocation to bonds, while maintaining the current level of risk. The Board assesses many asset mix scenarios, including their risk levels, before selecting a policy asset mix for the Plan.

8) Is the value-added for MEPP investment performance gross or net of investment fees?

   They are net value-added.

9) Why didn't the Board wait to recommend the reduction of contribution rates until the Plan is fully funded?

   Intergenerational equity is a concern when the current membership is paying for the unfunded liabilities. A special payment of past years losses amortized over 15 years, similar to a mortgage payment, of 4.65% ended on December 31, 2016. This payment is *past not current costs, and why the total contribution rate was reduced from 4.65% to 30%.*

10) How do the Plan's investment strategies affect the Plan's funded status? Did the Board build any buffer to maintain or decrease risks associated with the Plan?

    The Plan is mature but stable, and is able to absorb some negative outcomes. The Board focuses on the Plan's long-term sustainability and is forward thinking when managing risks associated with the Plan. The Board does not want to become overly conservative and wants to maintain the current risk levels, diligently monitored, to gain the best returns possible.

October 27 MEPB Stakeholder Governance Session Q & A

Afternoon Session Segment 1: 1:00 – 2:00 PM

1) What defines the Plan's mature state?

   Upon maturity, the number of contributors to the Plan's fund is reduced, and the number of pensioners grow. This ratio reaches or even tips past a point of equality. MEPP is approaching a stable state, where the number of active members and pensioner is almost equal. The Plan's maturity leads to greater risk and liability. The Board conducts actuarial analysis to monitor the Plan's maturity, and develops investment strategies to help maintain funding ratios.

2) The Plan investment information is showing negative cash flow. Does this mean that benefit payments are more than contributions? What has been done to manage the Plan's negative cash flows?

   The majority of the negative cash flow amount shown in the second quarter of 2017 is due to the Plan Administrator's new pension system upgrade, which caused a backlog of termination payouts. The Plans administrator is working to catch up on these termination payments.

   The Board has a conservative margin built into the actuarial assumptions to stabilize contribution rates fluctuation. In addition, the Board has made recommendations to the Minister regarding termination payment methodologies.

3) What are the actual investment fees paid to AIMCo? What is the percentage of contributions to cover these investment costs? Are these fees transparent?

   Every year, AIMCo participates in a CEM Benchmarking Survey, facilitated by a Toronto-based global benchmarking company, which conducts a comprehensive analysis of AIMCo's investment performance, risk, and costs compared to its peer group. MEPP's peer group, such as Telus Corporation, University Academics Pension Plan, University of Montreal Pension Fund, Saskatchewan Healthcare Employees' Pension Plan, are selected based on plan size because size is the primary driver of costs. Investment costs are adjusted to reflect the Plan's asset mix. AIMCo's costs are favorable compared with its peers.

   The fees are identified annually in the Plan's annual report. The 2016 MEPP Annual Report contains detailed information on AIMCo's costs on page 16.

4) What has been done to protect the Plan's bond and real estate portfolios in a rising interest rate environment?

   AIMCo is responsible for their investment strategies and has sound strategies in place.

   The Board conducts an ALS annually to monitor and measure risks and to identify an appropriate asset mix for the Plan. The bull market will end sometime and bonds are not attractive given the rising interest rates. The Board believes in diversification, and plans to reduce fixed income allocation and increase asset allocation in alternative asset classes. Real estate generates higher returns compared to bonds. Despite infrastructure's sensitivity to rising interest rates, AIMCo manages its infrastructure portfolios and risks well.

5) The ratio of contributing members to members drawing pensions is close to 1:1. What will happen when contributing members continues to decrease? Will this endanger the future pension benefits?

   Managing a mature pension plan can be challenging and the Board has built a margin for conservatism in funding to ensure its long-term sustainability. The Board is aware of the Plan's liquidity needs and monitoring.

6) Why didn't MEPP members receive communications regarding to the total contribution rate reduction? Why did the employer take all the contribution reduction?

   The Board makes recommendations to the Minister on the total contribution rate of the Plan. The Minister consults with his staff, and, makes a recommendation on how to split the employer (ER) and employee (EE) contributions to Cabinet. Cabinet then sets the new MEPP ER and EE contribution rates by order in council.

Afternoon Session Segment 2: 1:48 – 2:00 PM

1) Given the Plan's close tie with the PSPP, what is the relationship between the MEPB and PSPB? Does the PSPB host a stakeholder meeting?

   MEPP and PSPP are separate plans, managed and governed independently.

   The Chairs and/or Vice-Chairs of LAPB, PSPB, MEPB and SFPB meet quarterly (joint-chair meetings) to exchange information and address common concerns. The joint-chairs meeting is a forum for information sharing but not decision making since each plan has its own unique characteristics and challenges, and each board has different priorities and preferences.

2) The sustainability for public sector pension plans was a major concern in 2013 and 2014. How about now? What has been changed?

   The market conditions and macroeconomic environment have improved since 2013/14. The Board has done significant work to improve the overall financial health of the Plan. The Board has engaged the Plan's actuary, investment consultant, and investment manager to conduct an annual ALS. This ALS helps the Board better understand the risks associated with the Plan, optimize the asset mix, and develop appropriate investment strategies to ensure the long-term sustainability of the Plan.

   The Plan's fund has generated investment return over 10% for the past few years, which has improved the Plan's funded status.

The Board is about to complete the 2017 ALS and will update the MEPP Investment Policy (IP) and asset mix; however, it does not expect drastic changes to the Plan's asset mix.

3) More managers are retiring; however, the GoA will not hire new managers and continues to reduce the number of management positions. We heard a few years ago that the Plan's funds would be amalgamated. Is MEPP safe from future pension reform? Is our pension secure in future?

   The Board was and is not aware that there were any plans to amalgamate plan assets amongst the public sector plans, then or now. They are very different plans. The GoA's intent in 2013/14 was to close the Plan to new members and make some plan design changes. The Board is not aware of any drastic changes to the Plan benefits or any upcoming pension reform. In the 2013/14 public sector pension plan reform, the GoA proposed to close MEPP, and have new managers join PSPP.

   The Board cannot predict future regulatory changes, but the 2013/14 pension reform reminds the Board of what could happen. The Board relies on AIMCo's investment performance reports, stress test results, an annual ALS, and actuarial reports such as, cash flow data, annual extrapolations, and valuations to monitor the Plan's overall financial health. The Board also built conservatism into the actuarial valuation to avoid contribution rate fluctuation.

   The Board cannot guarantee that MEPP is immune from future pension reform; however, the Board is taking a proactive approach to address risks associated with the Plan, such as longevity risk, the Plan's maturity, affordability, and improving the funding status.

   A closed Plan would require a different asset mix and the risks and returns would be problematic.

4) Will the current MEPP members be grandfathered if the Plan is closed?

   In the 2013/14 public sector pension reform, the GoA recommended that new managers join PSPP but existing MEPP members would remain in the closed MEPP.

5) Are our pension benefits guaranteed? If the GoA wants to change my pension benefits, I would like to do my due diligence and be prepared for any upcoming changes.

   Pension benefits are defined in the legislation and rules, which are subjected to change. The Minister must consult with the Board on plan design changes. However, the GoA can change pension legislation.

   There is a provision in the MEPP legislation to protect members' pension benefits; it states that plan benefits cannot be retroactively changed. Benefits that members already earned, cannot be taken away. If pension benefits were to change, it would be on a go-forward basis.

   At present, the Board is not aware of any upcoming changes to pension benefits or other concerns.

6) Why did the Board recommend the total contribution rate reduction? Why didn't the Board wait until the Plan is 100% funded?

The Board completes an actuarial valuation every 2 years and must file a valuation at least every 3 years. The Board makes a recommendation to the Minister on the total contribution rate of MEPP. Treasury Board and Finance makes a recommendation to Cabinet and Cabinet sets the EE/ER contribution rate split, which is then approved by an order in council.

Contribution requirements for funding are determined by the ***normal*** *cost (current without costs for previous year's losses) of the Plan. A special payment of 4.65% towards the Plan's unfunded liability ended on December 31, 2016; therefore, the Board recommended a reduction of total contribution rate from 34.65% to 30%, effective February 1, 2017.*

To ensure intergenerational equity, the Board does not want to keep the contribution rates high for the current membership paying for past losses.