SHARED RISK PLAN FOR CUPE EMPLOYEES OF NEW BRUNSWICK HOSPITALS

FUNDING POLICY

As amended to June 5, 2014

Amended October 20, 2016

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SECTION I – PURPOSE OF PLAN AND FUNDING POLICY

The purpose of the Shared Risk Plan for CUPE Employees of New Brunswick Hospitals (the **"Plan"**) is to provide secure pension benefits to members and former members (collectively **"members"**) of the Plan without an absolute guarantee, but with a risk focused management approach delivering a high degree of certainty that base benefits can be met in the vast majority of potential future economic scenarios.

The primary focus is to provide a highly secure lifetime pension at normal retirement age. However, the intention is that additional benefits may be provided depending on the financial performance of the Plan. Benefit objectives are discussed in Section II.

The Funding Policy is the tool used by the Board of Trustees to manage the risks inherent in a shared risk plan. The Funding Policy provides guidance and rules regarding decisions that must, or can, be made by the Board of Trustees around funding levels, contributions and benefits.

A shared risk plan is based on the principle that the management of risks for a pension plan over time can best be achieved through actions on both sides of the balance sheet (i.e., liabilities and assets). This funding policy describes the timing and the actions that the Board of Trustees must take, or consider, as applicable, based on the results of the funding policy valuation of the Plan and the application of the required risk management procedures to the Plan.

In addition, the Board of Trustees must regularly monitor the economic, demographic and pension environments and make adjustments, where allowed, or provide recommendations to the Province and Union as and when these are necessary to maintain the Funding Policy current in a changing world.

Capitalized terms used in this Funding Policy that are not defined herein have the meaning given to such terms in the Plan.

SECTION II – BENEFIT OBJECTIVES

Prior to the conversion to a shared risk plan, the Plan provided defined benefits based on a five year average salary formula at retirement and included post-retirement indexing at a fixed rate of 2%.

The primary benefit objective for the Plan is to deliver benefits that closely replicate, to the extent possible, the benefits provided under the Plan prior to the conversion, including inflation protection.

The nature of a shared risk plan is such that these objectives are not guaranteed. However, contributions have been set at a level such that there is a good chance of delivering on the primary benefit objective, if there is a reasonable investment performance.

Furthermore, benefit accruals under the Plan after the conversion are based on a normal retirement age of 65 with a 5% per year reduction for early retirement. This change reflects anticipated continued increases in life expectancy. The overall plan design objective with respect to retirement age is to provide each cohort of plan members with about the same expected number of years of pension payments for a similar amount of pension in current dollars at retirement.

None of the above are guarantees. These benefit objectives can only be met if the contributions and Plan experience, most importantly investment performance, allow this to happen. However, the above provide guidance on the benefit objectives that underlie the Plan design.

SECTION III – RISK MANAGEMENT

The Plan was designed to achieve or exceed the risk management goals prescribed under Regulation 2012-75 (the **"Regulations"**) to the New Brunswick *Pension Benefits Act* (the **"Act"**) (the Regulations and the Act are collectively referred to as the **"PBA"**). Certain procedures were developed to test whether these goals can be achieved given the contribution rules and benefits defined in the Plan. These goals and procedures are described separately below.

GOALS

The primary risk management goal is to achieve a 97.5% probability that base benefits will not be reduced over the following 20 years.

The goal is measured by taking into account the following funding management plans:

1. the funding deficit recovery plan except for reduction in past or future base benefits, and
2. the funding excess utilization plan excluding permanent benefit changes.

The funding deficit recovery plan and the funding excess utilization plan are described in Sections V and VI, respectively.

There are two secondary risk management goals. These are:

- On average provide contingent indexing on base benefits (all members) that are in excess of 75% of CPI over the next 20 years.
- Achieve at least a 75% probability that the ancillary benefits described in the Plan text at conversion can be provided over the next 20 years.

For the purposes of meeting these goals, base benefits include the accrual of extra service of members and any contingent indexing provided based on the financial performance represented by each scenario tested.

If as a result, through the testing process, a scenario allows for indexing in a given future year, then this contingent indexing amount becomes part of the base benefits that is to be protected.

PROCEDURES

The risk management goals are measured using an asset liability model with future economic scenarios developed using a stochastic process.

The model is run with at least 1,000 alternative economic scenarios over 20 years. For each of these scenarios and for each year, the financial position of the Plan is measured. For each of these measurements, a decision consistent with the funding deficit recovery plan or the funding excess utilization plan, as applicable, is modeled with the exceptions noted under the goals above. This provides at least 20,000 observations from which to measure whether the risk management goals have been achieved.

An asset liability model using a stochastic process requires that a number of important modeling assumptions be made. These assumptions are described below:

- The economic assumptions are developed for each asset class and for key economic parameters based on a combination of past experience, current economic environment and a reasonable range of future expectations. These assumptions are reviewed annually and updated as required. They are also subject to approval by the Superintendent of pensions (the **"Superintendent"**).
- The Plan's contributing member population is assumed to be stable in each year of the projection period. As such, each departure from the Plan, for any reason, is assumed to be replaced by a new entrant. The new entrant population reflects the profile of new Plan members expected in the future based on Plan experience. If required under subsection 100.7(3) of the PBA, the assumption regarding the contributing member population may be altered.

All risk management goals were tested at the Conversion Date. In addition, the primary risk management goal will be tested annually. The result of this test combined with the results of the funding policy valuation at the same date will determine the actions the Board of Trustees are required to take, or can consider, under the terms of this Funding Policy.

The primary risk management goal must be achieved or exceeded:

- At July 1, 2012 (i.e. the Conversion Date);
- At the date a permanent benefit change as defined in the Regulations is made;
- At the date a benefit improvement as defined in the Regulations is made; or
- At the date the contribution adjustments are fully implemented.

The secondary risk management goals must be achieved or exceeded:

- At July 1, 2012 (i.e. the Conversion Date); or
- At the date a permanent benefit change as defined in the Regulations is made.

The definitions of permanent benefit change and benefit improvement are as follows:

"permanent benefit change" means a change that is intended to permanently change the formula for the calculation of the base benefits or ancillary benefits after the date of the change, including a change made in accordance with the funding excess utilization plan.

"benefit improvement" means an escalated adjustment for past periods or an increase in other ancillary benefits allowed under the funding policy.

SECTION IV – CONTRIBUTIONS

The contributions required by the Plan include the initial contributions and contribution adjustments as may be required by the Funding Policy.

INITIAL CONTRIBUTIONS

The initial total contribution rate shall not be less than 19.1% of earnings as defined in the Plan text. The initial contribution rate for members shall be 9%. These contributions are to remain the same unless altered by:

- Contribution adjustments triggered under the Funding Policy;
- An additional reduction required under the *Income Tax Act* (Canada) (the **"ITA"**) (references in this Funding Policy to the ITA shall include the regulations thereunder where the context requires);
- A permanent benefit change resulting in a contribution rate change as may be agreed by the Province and the Union and subject to the requirements of the PBA and the ITA;
- Other changes to the Plan beyond those contemplated by this Funding Policy and only if agreed to by the Province and the Union and subject to the requirements of the PBA and the ITA.

CONTRIBUTION ADJUSTMENTS

Contribution adjustments may be made by the Board of Trustees based on the conditions set out below.

An aggregate contribution increase of up to a total of 1% of earnings can be triggered by the Board of Trustees if the open group funded ratio of the Plan, as defined by the PBA, falls below 100% for two successive year ends. The amount of the increase up to the limit of 1% shall be such that the primary risk management goal is achieved and such that the open group funded ratio is at least 105% as required by the PBA. If the primary risk management goal and 105% open group funded ratio cannot be achieved, the increase shall be 1% of earnings.

The contribution increase shall take effect no later than the first complete pay period that is within 12 months following the funding policy valuation date that triggered the need for the change (i.e. no later than 12 months after the funding policy valuation date). The contribution increase shall be removed at the end of the year in which the results of the previous funding policy valuation reveal that the open group funded ratio reaches 105% without considering the effect of the contribution increase and the primary risk management goal is met.

A reduction in contributions of up to a total of 2% of earnings can be triggered by the Board of Trustees if the conditions set forth in the funding excess utilization plan in Section VI are met. The amount of the reduction shall be such that the primary risk management goal can still be met after the reduction in contributions. The contribution reduction shall take effect no later than the first complete pay period that is within 12 months following the funding policy valuation date that triggered the need for the change (i.e. no later than 12 months after the funding policy valuation date). The reduction in contributions shall be removed when the open group funding level falls below 140% for two successive year ends.

INCOME TAX ACT LIMIT

In the event that all actions contemplated under the funding excess utilization plan in Section VI have been implemented and the eligible contributions still exceed the limit allowed under the ITA, then the contributions shall be further reduced to the limit allowed under the ITA.

SHARING OF CONTRIBUTIONS

The initial contribution rate of at least 19.1% is composed of 9.0% from contributing members and at least 10.1% from the Province. Contribution holidays may only be taken in the event they are required under the ITA. In the unlikely event that the ITA required a contribution holiday, the contribution holiday would apply equally to both members and the Province up to the point where no contributions are required from members (i.e., reductions in contributions of up to 18% would be shared equally between the members and the Province). If additional contribution reductions are required, then the balance of the Province's contributions would also be reduced until they reach zero.

Other than as noted above for contribution holidays, any contribution adjustment shall be shared 50/50 between the members and the employer, subject to the ITA.

EXPENSES

All expenses pertaining to the administration of the Plan shall be paid by the Plan. For the purposes of the risk management procedures, the funding policy discount rate is set net of Plan investment expenses. Plan administration expenses are reflected in the normal cost.

SECTION V – FUNDING DEFICIT RECOVERY PLAN

The funding deficit recovery plan must be implemented by the Board of Trustees if the open group funded ratio of the Plan falls below 100% for two successive plan year ends.

Once triggered, a report shall be provided to the Superintendent describing how the Board of Trustees is dealing with the underfunding of the Plan. In addition, Plan members, the Province and the Union shall be informed of the actions being taken and the effect and timing of these actions on the contributions and benefits.

The funding deficit recovery plan shall consist of the following actions in the order of priority as listed below:

1. Increase contributions as allowed in Section IV; provided that with respect to increases to member contributions a waiver under subsection 8503(5) of the regulations to the ITA is attained;

2. Change early retirement rules for post-conversion service for members who are not yet eligible to retire and receive an immediate pension under the terms of the Plan to a full actuarial reduction for retirement before age 65;

3. Change early retirement rules for pre-conversion service for members who are not yet eligible to retire and receive an immediate pension under the terms of the Plan to a full actuarial reduction for retirement before age 60;

4. Reduce base benefit accrual rates for future service after the date of implementation of the deficit recovery plan by not more than 5%;

5. In addition to the reduction in step 4 above, reduce base benefits on a proportionate basis for all members regardless of membership status for both past and future service in equal proportions.

The above actions shall be taken one by one and when the primary risk management goal is met, no further actions are required at that time. Further actions are triggered when the primary risk management goal cannot be achieved with the cumulative effect of all previous actions, such goal being measured annually and follow-up actions to take effect as per the timelines below.

For example, if the funding deficit recovery plan is triggered, the Board of Trustees would implement step 1 first and conduct the primary risk management goal test. If step 1 is sufficient to meet the primary risk management goal, no further action would be required at that time. At the next annual review, the goals would be tested again and if not achieved, steps 2, 3 and 4 in succession would be implemented in the same manner and under the same circumstances as step 1.

If steps 1 through 4 are not sufficient to achieve the primary risk management goal, base benefit reductions for all members must be implemented.

The base benefit reduction, if required, shall be such that both goals below are achieved:

1. 105% open group funding level; and

2. Primary risk management goal of 97.5% probability that base benefits need not be further reduced over the next 20 years.

The measurement date is the funding policy valuation report date that triggered the need for the action or actions taken under the funding deficit recovery plan.

The timing of the changes shall be as follows:

- For steps 1 through 4, no later than 12 months following the date of the funding policy valuation report that triggered the need for the action.

- For step 5, no later than 18 months following the date of the funding policy valuation report that triggered the need for base benefit reductions.

SECTION VI – FUNDING EXCESS UTILIZATION PLAN

The funding excess utilization plan describes the actions the Board of Trustees must take or consider when the open group funding levels exceeds 105%. If the open group funding level is at 105% or less, there are no actions that can be taken under the funding excess utilization plan.

EXCESS AVAILABLE FOR UTILIZATION

The amount available for utilization is as follows:

1. 1/6th of the excess funds that make up the difference between the open group funding level at the valuation date to a maximum of 140% and 105%; PLUS
2. 100% of the excess above 140%.

The actions that can be taken depend on whether the base or ancillary benefits have ever been reduced and such reduction not subsequently reversed and on the priority order set out below.

BASE OR ANCILLARY BENEFITS REDUCED AND NO REVERSAL

If base benefits and/or ancillary benefits have been reduced, all excess available for utilization must first be used in the following order of priority:

1. Base benefit reductions (with respect to both past base benefits and future base benefits) must be reversed with respect to future payments after the date of reversal until all the previous reductions to base benefits have been eliminated.
2. Reductions in ancillary benefits (with respect to both past ancillary benefits and future ancillary benefits) other than contingent indexing must be reversed with respect to future payments until all the previous reductions have been reversed.

OTHER ACTIONS

If base benefits and/or ancillary benefits have never been reduced or after all previous reductions have been reversed for future payments, then the Board of Trustees may take the following actions with respect to the excess available for utilization. Such actions shall be taken in the following order of priority and no action can be taken until the immediately preceding action in the list below has been fully implemented:

1. Provide indexing of base benefits and accrued bridge benefit up to the full CPI since the last date where full CPI was achieved. The percentage increase shall be the same for all members subject to an individual limit of recovery of full CPI up to January 1 of the year that follows the valuation date or coincides with it if the date of the valuation is January 1st of the same year.
2. Provide further increases in base benefits of members who were not in receipt of a pension at the actuarial valuation report date that triggered the action. This increase shall be such that the base benefits are upgraded to a final five year average as at the same date (or such shorter averaging period as applicable for those with less than 5 years of service at that date).

3. Provide a further increase to retired members such that a final average formula is reasonably replicated for each retired member at their retirement date and indexed to full CPI thereafter subject to any limitation imposed under the ITA.
4. Provide a lump sum payment representing a reasonable estimate of missed past increased payments up to the levels of benefits arising out of steps 2 and 3.
5. Provide a further increase to benefits of members who were not in receipt of a pension at the funding policy valuation date that triggered the action up to the rate of increase in the average wage or such other reasonable measure as may be determined by the Trustees subject to Section 8504 of the regulations to the ITA; provided that no such increase would result in a requirement to calculate Past Service Pension Adjustments.
6. Establish a reserve to cover the next 10 years of potential contingent indexing.
7. Apply contribution adjustments of up to 2%, as allowed under Section IV.
8. Provided that contribution adjustments of 2% have been made in accordance with action 7 above, improve the normal form of pension for all members who are not in receipt of a pension.
9. Improve the bridge pension for all members eligible for a bridge pension whether or not in pay.
10. Improve the early retirement rules for service after June 30, 2012, provided that the Board of Trustees considers life expectancy experience as it develops.

Actions 1 to 5 can be applied with excess funds available when the open group funded ratio is below 140%. If some residual excess remains available after providing maximum allowed increases under the ITA for actions 1 to 5 above, such excess shall remain in the fund as increased security against future potential downturns in experience.

If all improvements from 1 through 5 above have been made and the open group funded ratio is still in excess of 140%, then actions 6 through 10 can be undertaken in sequence. After such actions have been undertaken, the Trustees may consider permanent benefit changes subject to the approval of the Province and Union and subject to most members being able to benefit from the changes.

If all of the actions above still leave the Plan with contributions in excess of the ITA limits, then reduce contributions to the maximum allowed under the ITA.

Each of the actions above can only be implemented after confirming that the primary risk management goal is achieved after the change is made. In addition, steps 6 to 10 can only be implemented if the secondary risk management goals are also met.

Except for the timing of contribution reductions (described in Section IV), the timing of the above actions shall be the first of the year that is 12 months after the date of the funding policy valuation report that triggered the actions.

SECTION VII – ACTUARIAL ASSUMPTIONS

A funding policy actuarial valuation shall be conducted by the Plan's actuary at December 31st of each year. The actuarial assumptions used for the funding policy valuation and factors to consider regarding changing such assumptions are discussed in this section.

Each assumption is discussed under separate headers below.

DISCOUNT RATE

Effective December 31, 2015, the discount rate shall be 4.50% per annum.

On the advice of the Plan's actuary, the Board of Trustees may consider a change in the discount rate for subsequent funding policy actuarial valuations.

The intent is to leave the discount rate stable. Subject to the foregoing, the discount rate may be changed if required by the Superintendent, standards published by the Canadian Institute of Actuaries, applicable laws or if there are changes in the economy that in the Plan's actuary's opinion warrant a change in the discount rate.

MORTALITY

In order to take into account the improvements in life expectancy recently substantiated by the Canadian Institute of Actuaries in its report on Canadian Pensioners Mortality (published on February 13, 2014), the CPM-2014Publ Mortality Table and the CPM-B Improvement Scale, which varies by gender, age and calendar year is to be used. Adjustment factors of 131.0% and 123.0% for males and females, respectively, are also applied to the mortality table to take into account the level of pensioner benefits among plan beneficiaries, as well as the expected mortality for employees in the medical and social services industry relative to the general public sector. The same adjustments are to be used for all members before and after retirement.

The mortality basis shall only be changed if required by the Superintendent or the Canadian Institute of Actuaries to reflect improvements in life expectancy beyond those contemplated by the last table used or if recommended by the Plan actuary to reflect even greater improvements in life expectancy.

RETIREMENT PATTERNS

The retirement patterns shall reflect Plan experience modified to allow for anticipated changes due to changes in early retirement rules.

The retirement patterns shall be reviewed at least every five years and changed to reflect emerging experience.

TERMINATION RATES

The termination rates developed for the former CUPE Hospitals Plan were used for the Plan. There is no reason to believe that the introduction of the shared risk model will impact significantly the termination of employment behavior of plan members, and determined that the table used in the past continues to be appropriate.

This assumption will be reviewed periodically and changed, as deemed appropriate.

SECTION VIII – ANNUAL REVIEW

The annual review of the Funding Policy consists of two elements as follows:

1. Process for application of the Funding Policy; and
2. Identification of potential changes to the Funding Policy that may be required.

APPLICATION OF FUNDING POLICY

The Funding Policy shall be applied as follows:

1. Funding policy valuation report at December 31st of each year.
2. Risk management procedure conducted as at the valuation date each year.
3. Calculation of the open group funded ratio.
4. Identification of Trustee action or actions required or possible under this Funding Policy.
5. Test of risk management goals as required under the Funding Policy after change in step 4 and if met, step 4 can be implemented.
6. If test in step 5 not met, then change in step 4 adjusted under the terms of the Funding Policy such that the risk management goals required to be met under the terms of this Funding Policy are met.
7. Report to Superintendent and fulfill any other PBA requirements.
8. Report to members, Province and Union.

IDENTIFICATION OF POTENTIAL CHANGES

The Board of Trustees shall annually review the terms of this Funding Policy to identify changes required to either improve clarity of the Funding Policy or remain current with changing Plan, pension environment, demographic or economic circumstances.

The following changes may be made by the Board of Trustees:

(i) Changes that are needed to comply with a law or regulation; and

(ii) Subject to (i), changes that are not related to or do not affect the Parameters set out in Schedule “A”.

All other changes must be approved by the Province and the Union and ultimately the Superintendent.

SCHEDULE A

<u>The Parameters</u>

- Initial Contributions
- Contribution Adjustments
- Sharing of Contributions
- Funding Deficit Recovery Plan (Section V)
- Funding Excess Utilization Plan (Section VI)