

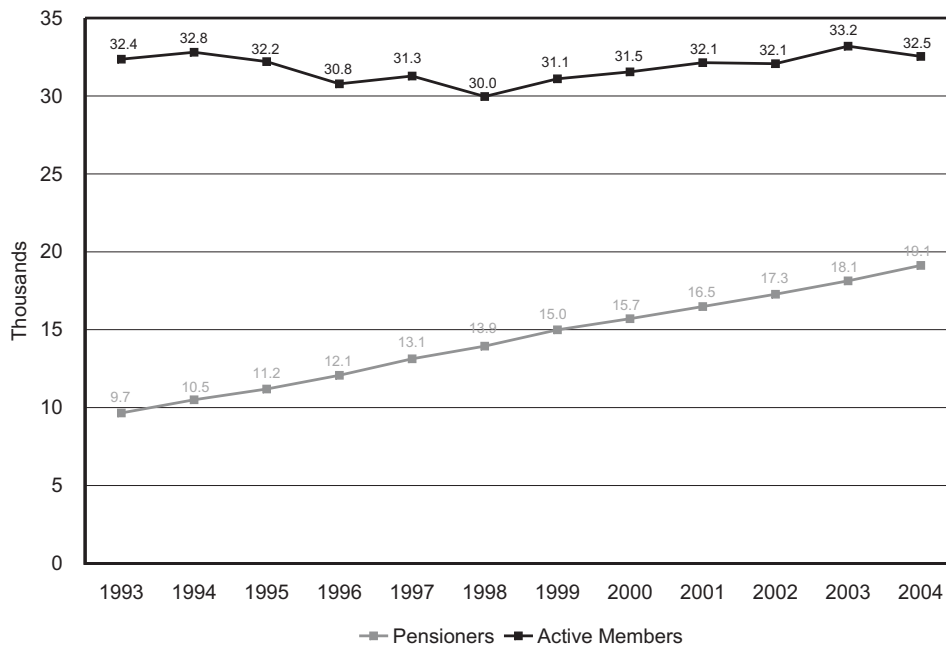
5.1 Retirement Benefits - Pensions

Prior to 1967, public service salaries and pension benefits were paid under the authority of the *Civil Service Act*. Under that legislation there were no employee or employer contributions to a pension plan and pension benefits were paid out of the Consolidated Revenue Fund. In 1967, legislation was enacted which required that employees contribute to a pension plan. Employees' pension premiums were paid into the Consolidated Revenue Fund and pension benefits continued to be paid out of it.

In 1981, legislation was enacted which created the Province of Newfoundland and Labrador Pooled Pension Fund and required that employee and employer pension premium contributions be paid into the Fund. Subsequent to the establishment of the Fund, pension benefits were paid by the Fund irrespective of whether the employee had contributed pension premiums to it. Figure 1 provides historical data for the Fund relating to pensioners and active members for the past 12 years.

Figure 1

**Province of Newfoundland and Labrador Pooled Pension Fund
Population History: Pensioners and Active Members
Years Ended 31 December
(000's)**



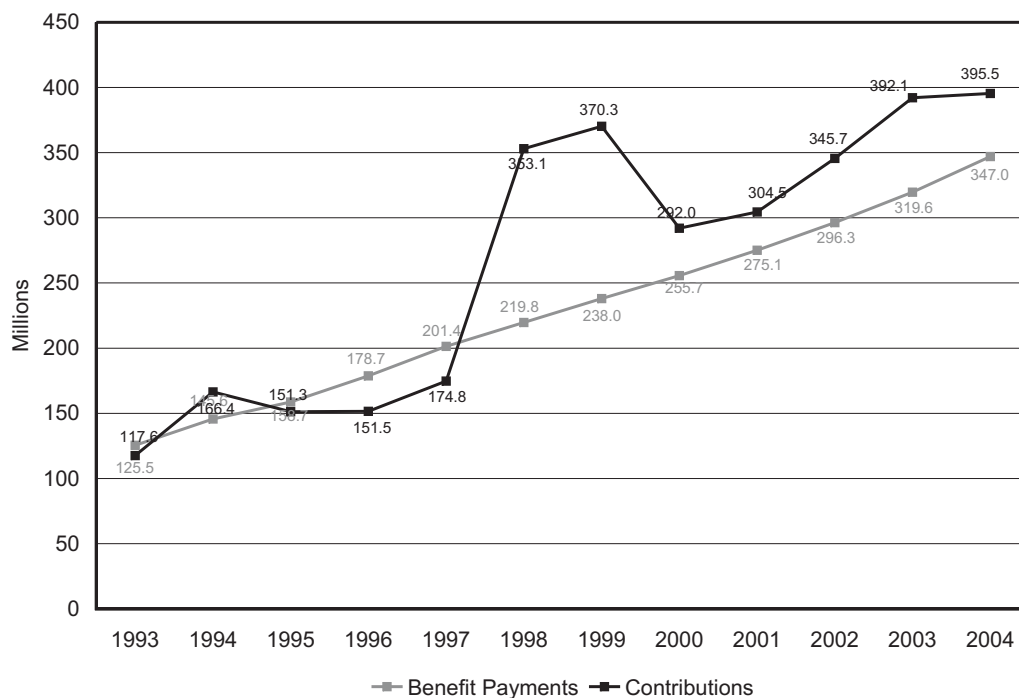
Comments on Selected Financial Information and Other Matters

At 31 December 2004, the Province of Newfoundland and Labrador Pooled Pension Fund was comprised of five pension plans: the Public Service Pension Plan, the Teachers' Pension Plan, the Uniformed Services Pension Plan, the Members of the House of Assembly Pension Plan and the Provincial Court Judges' Pension Plan. All employee and employer contributions are deposited into the Fund and pension benefits to plan members and other pension payments are made from it.

Our review disclosed that for the year ended 31 December 2004, approximately 32,500 employees, Members of the House of Assembly, and the employer paid pension premiums totalling \$395.5 million into the Pension Fund under the five pension plans. Premiums of \$395.5 million include a \$163.5 million contribution by Government in excess of matching provisions. During the same period, the Fund provided benefits totalling \$347.0 million to approximately 19,100 retirees. Figure 2 provides historical data for the Fund relating to pension benefits paid and pension contributions received for the past 12 years.

Figure 2

Province of Newfoundland and Labrador Pooled Pension Fund Pension Benefit Payments and Contributions Years Ended 31 December (\$ Millions)

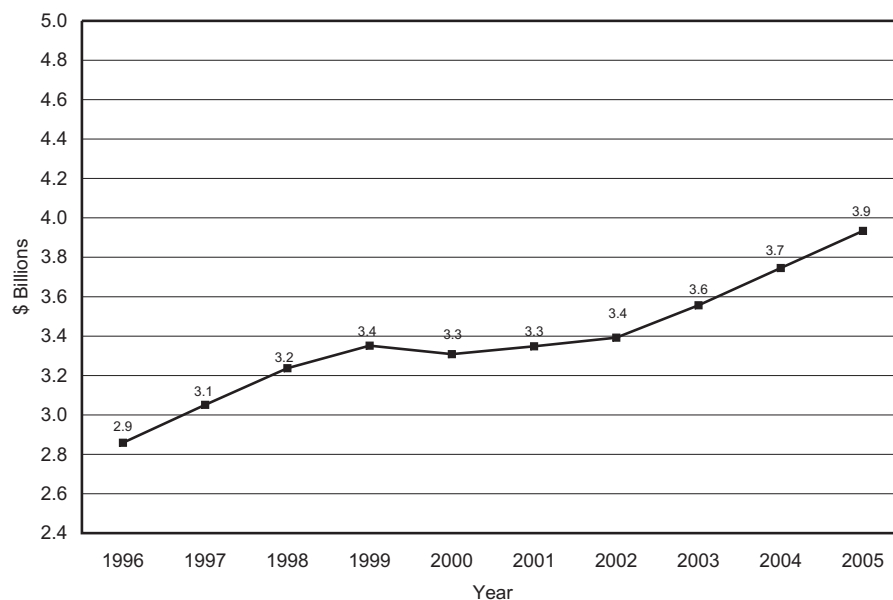


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The unfunded pension liability represents a significant debt for Government which at 31 March 2005 was \$3.9 billion. Information on the unfunded liability as at 31 March for the years ended 1996 to 2005 is outlined in Figure 3.

Figure 3

Consolidated Summary Financial Statements Unfunded Pension Liability As at 31 March (\$ Billions)



Commencing during the 1997-98 fiscal year, Government started to make special payments to the Public Service Pension Plan to address the unfunded liability. Government contributed \$30 million in each of 1997-98 and 1998-99, \$40 million in each of 1999-2000, 2000-01 and 2001-02, \$45 million in 2002-03, and \$60 million in 2003-04 and 2004-05. Government's contribution will continue at \$60 million until the unfunded liability is extinguished. In addition, Government increased the contribution rate for employees and employers by 1.0%, which was in effect as of January 2000.

During 1998-99, Government negotiated a collective agreement with the Newfoundland and Labrador Teachers' Association which included provisions to address the unfunded liability of the Teachers' Pension Plan. In accordance with the agreement, Government will contribute up to \$815 million to the Plan over a 14 year period. Government paid \$166 million towards this commitment in 1998-99 and 1999-00 and paid

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\$76 million in each fiscal year from 2000-01 to 2004-05. Additional annual payments are to be made in instalments of \$76 million until the remaining balance of an initial obligation of \$815 million, plus interest, has been paid. However, even with these additional payments, the Province's actuary has indicated that the Teachers' Pension Plan is expected to run out of funds in 2014. Once the Fund is exhausted, the negative cash flow will then become the amount Government will have to pay in order for plan members to receive their pensions. The initial deficiency amount Government will have to pay is \$196 million and this deficiency amount will increase to a maximum of \$255 million in 2026.

As at 31 March 2005, the unfunded liability for the Uniformed Services Pension Plan was \$175.4 million and was estimated to increase to \$396 million by 2030. In 2001-02, the Province agreed to a five-year commitment to provide an annual payment of \$20 million to the Uniformed Services Pension Plan.

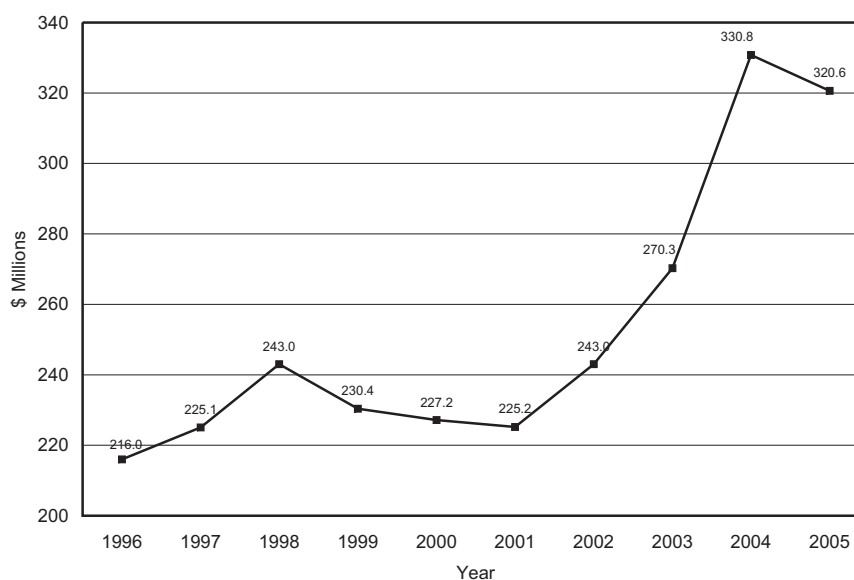
As at 31 March 2005, the unfunded liability for the Members of the House of Assembly Pension Plan was \$40.3 million and was estimated to increase to \$87 million by 2033. In 2001-02, the Province agreed to a five-year commitment to provide an annual payment of \$7.5 million to the Members of the House of Assembly Pension Plan. In 2003-04, Government decided to cease these annual payments as a result of requirements of the *Income Tax Act*.

During 2003-04, pensions of certain Provincial Court Judges were moved from the Public Service Pension Plan to a new Provincial Court Judges' Pension Plan. As at 31 March 2005 the plan had an estimated unfunded liability of \$3.2 million. The Plan consists of two components, a registered component and a supplementary component. The registered component, which will continue to be administered within the Province of Newfoundland and Labrador Pooled Pension Fund, provides for contributions and benefit payments based on limits set out in the federal *Income Tax Act*. The supplementary component will be administered in the accounts of the Consolidated Revenue Fund and will provide for contributions and benefit payments in excess of the *Income Tax Act*.

While Government has taken action to address the unfunded liability of its pension plans, the net unfunded liability, including unamortized experience gains and losses, continues to increase. As at 31 March 2005 the unfunded pension liability was \$3.9 billion, an increase of \$188.1 million from the balance of \$3.7 billion as at 31 March 2004. The liability increased even though Government made special payments totalling \$156.0 million. One of the main reasons for the increase in the unfunded liability was the significant interest costs associated with the unfunded pension liability. The interest costs relating to the pension plans each year since 1996 are outlined in Figure 4.

Figure 4

**Consolidated Summary Financial Statements
Interest Costs on the Unfunded Pension Liability
Years Ended 31 March
(\$ Millions)**



As Figure 4 indicates, in recent years there has been a significant increase in interest costs associated with the Province's unfunded pension liability. In 1996, interest costs amounted to \$216.0 million while in 2005, interest costs were \$320.6 million, an increase of \$104.6 million or 48%. One of the most significant factors contributing to the increase in interest costs is the correlation between interest costs and the balance of the unfunded pension liability. For example, in 1996, the unfunded pension liability was \$2.9 billion, while in 2005, the unfunded pension liability was \$3.9 billion, an increase of \$1.0 billion or 35%.

Recommendation

Government should continue its efforts to address its unfunded pension liability.