UNIVERSITY OF REGINA
ACADEMIC AND ADMINISTRATIVE BENEFITS COMMITTEE
ANNUAL REPORT
for the year 1998

Errors of commission and omission excepted. This is not a legally binding version of this document.

About the Academic and Administrative Pension Plan

The Academic and Administrative Pension Plan was established on 1 July 1965. The plan is a defined-benefit plan, meaning that a member's pension is calculated using a formula based on the member's salary history and years of service at retirement. The plan also allows the transfer of entitlements — including the portion of the accumulated contributions contributed by the University — out of the plan upon retirement, death or resignation.

Membership in the plan is compulsory for academic and administrative staff. The plan currently has about 900 members, of whom about 20% are retired members receiving pension benefits under the plan.

Profile of the Committee

The Academic and Administrative Benefits Committee is a standing committee of the Board of Governors. The mandate of the Committee is to advise the Board on matters relating to benefit plans for academic and administrative staff, including:

- The Academic and Administrative Pension Plan
- The Group Life Insurance Plan
- The Salary Continuance Plan
- The Travel Insurance Plan
- The Dental Plan

Committee Web Site

Visit the AABC web site at http://www.cas.uregina.ca/~aabc/

Message from the Chair

The Academic and Administrative Benefits Committee had two main foci in 1998. The normal monitoring of the pension and benefits plans and the continuing review of the design of the pension plan. Both the stock markets and the course of the pension review had significant ups and downs during the year. However, I am pleased to report that, by the end of 1998, investment performance for the year was satisfactory and the pension review was approaching a conclusion.

The Academic and Administrative Benefits Committee (AABC) met twelve times during 1998. AABC members join members of the Committee on Employee Benefits, which oversees benefit plans for CUPE 1975 members, to form the Joint Investment Committee; this latter committee met five times during 1998. The Joint Investment Committee monitors the Master Trust Fund, which contains the assets of all three of the University's pension plans.

Investment performance is always a priority item for the Committee. After three consecutive years of double-digit returns, there was an expectation that 1998 might be a year of consolidation. If one just looks at the 1998 rate of return for the pension fund, which was 8.3%, it would appear that this expectation was fulfilled. But this simple number belies the financial crises, falling markets and blaring headlines of the late summer and early fall. Fortunately, a solid rise in markets late in the year brought the fund's 1998 rate of return solidly into positive territory. Over the past four years, the fund earned 14.9% on an annualized basis, just a hair below the fund's benchmark return of 15.0%. A more detailed analysis of the fund's assets and investment performance will appear later in this report.

The review of the design of the pension plan continued through 1998. There were false starts and false hopes in the process, but the Committee was confident that a conclusion was in sight as the year-end came. The review of insurance benefits went much more smoothly. The pension and benefits review process will be described in detail below.

Pension plan design is a very complicated issue. During the pension review, the Committee has been fortunate to have had the assistance of its actuarial consultants of record, Aon Consulting, and of consultants from William M. Mercer Limited, who were engaged for the specific purpose of facilitating the review. Special thanks go to David Keet and Louis Martel of Aon and to Jim Giesinger, Wes Peters and Gord Simle of Mercer.

It was a tough year to be an investment manager, especially during the middle part, but our primary investment managers, Phillips, Hager and North Limited of Vancouver, again helped the fund to achieve a reasonable rate of return. I offer the Committee's thanks to Tom Bradley of PH&N for remaining calm and holding the course during choppy

markets. It is a pleasure to pay tribute to the hard work and support of our colleagues Janet Julé, Jeff Stepan and John Myrah at James P. Marshall, Inc. for their assistance in monitoring investment performance, for advice about investment policy, and for drafting the investment review section of this report. The list of tributes would not be complete without an expression of gratitude to Bonnie Dobni and Louise Doan at Human Resources.

David Barnard left the Committee in July when he became President of the University, while Stu Mann left earlier in the year. The Committee congratulates David and wishes him well in his new role. Stu Mann was a prominent member of the Committee during his working days at the University and has served on the Committee twice as a representative of the retired members. Many thanks again, Stu! David and Stu's positions on the Committee have been assumed by Frank Proto and Norm Beirnes respectively.

R.J. Tomkins
Chair
April 1999

The Pension Plan

Review of 1998 Investment Performance

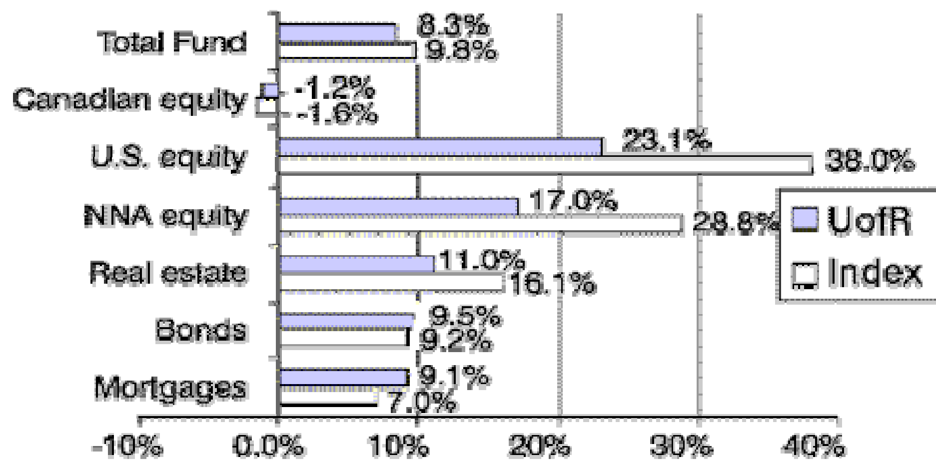
1998 provided an 8.3% return for the University Pension Plans.

Equity markets were volatile in 1998, as investors continued to absorb the fallout of the Asian crisis. After a very weak third quarter, the fourth quarter of this year was one of recovery, leaving the Toronto Stock Exchange (TSE) 300 Index slightly negative over the year. Foreign equity markets fared better. Particularly strong was the U.S. as represented by the large-cap Standard & Poors (S&P) 500 Index, which was up 38% in Canadian dollars. Europe led non-North American equity markets and by year-end the Europe, Australia, Far East (EAFE) Index was up close to 29% in Canadian dollar terms.

Bonds markets displayed some ups and downs, albeit without the extremes of the equity markets. Aside from a brief interlude in August, when interest rates were increased to protect the dollar from speculative pressure, the trend for interest rates was generally down in the year. As a result, the bond market as a whole experienced capital gains in addition to an income yield. The Scotia Capital Markets Universe Bond Index (SCMUBI) provided a 9.2% return for the year.

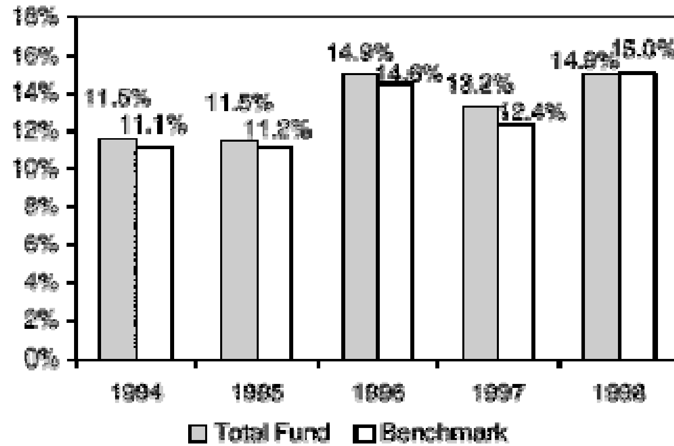
Against this market backdrop, the one-year return for the University of Regina Master Trust was 8.3%. This annual result trailed the 9.8% return on the benchmark portfolio, as set out in the Plan's investment policy. Relative performance was adversely affected by below-index performance in U.S. equities and non-North American equities. However, in absolute terms, the foreign equity exposure added value to the fund's performance, since foreign markets generally posted much higher returns than Canadian stocks and bonds, and since the fund's commitment to foreign equities was higher than the benchmark portfolio. Other positive factors include the Canadian equity, bond and mortgage returns, which all tracked slightly ahead of their respective indices. The chart that follows shows the total return and asset class returns relative to the benchmark and above noted index returns.

1998 Investment Performance



Over the longer term, the Pension Plan performance has been stronger relative to the benchmark objective. Over the past four years, the Total Fund return was 14.9%, tracking within 0.1% of the 15.0% benchmark return. Earlier rolling four-year returns tracked ahead of target, as the following chart reveals.

Academic Plan
Rolling 4-Year Returns



While the Master Trust trailed the benchmark objective in the year, the return fared well compared to other funds. The year-end result compared favorably with the median fund return of 7.6% in the Canadian Trust Universe Comparison Service (CTUCS). The University's result benefited from having a greater foreign equity exposure than the median fund. Holding real estate was also beneficial as that asset class posted its second consecutive year of double-digit returns.

Performance of the 85% of assets managed by Phillips, Hager and North Limited (PH&N) is compared in the following table to other funds in the CTUCS survey over the past year and four year periods.

1998 Relative Performance

Asset Class	1998 Percentile 1	4-Year Percentile 1
Canadian equities	52	54
U.S. equities	76	n/a 2
Non-N.A. equities 3	64	n/a 2
Foreign equities 3	70	49
Bonds	48	36
Mortgages	37	24
Total Fund	54	42

1 Indicates the percentage of funds in the CTUCS survey that reported **better** performance than the U of R fund. Small numbers signify excellent performance relative to other funds, while numbers close to 100 indicate poor relative performance.

2 Information not available.

3 Refers to assets managed by PH&N only.

The PH&N portfolio result fell just below the median fund over the past year. With the exception of foreign equities, asset class results were about average to slightly above average. Asset mix pulled down the relative ranking, as PH&N had higher exposure to Canadian equities and lower exposure to foreign equities than the median fund. It should be noted that PH&N's relatively low commitment to foreign markets is mainly due to federal restrictions on foreign content in pension funds and the fact that the Fund also has two specialty managers with international mandates. Over the past four years, the Total Fund and underlying asset class results were generally above the median fund results.

Investment Performance Objectives

A number of performance objectives are set out for the pension plans. The primary objective is that the Total Fund return exceed a benchmark portfolio return over rolling four-year periods.

The benchmark portfolio return is calculated by using index returns and asset class weights, which are currently: Canadian equities 38%; U.S equities 9%; Non North American equities 9%; Real Estate 3%; Bonds 39%; and short term investments 2%.

Within the various asset classes, the objective is to exceed the relevant index return. For Canadian and U.S. equities the return objective is at least 110% of the index return. For bonds and mortgages, the value added objective is 105%.

The pension plans also have a long term objective of earning a real return (net of inflation) of 3% per year.
In addition, the returns are evaluated on a relative basis to a universe of other pension plan returns.

The Master Trust

The assets of the University of Regina three pension plans - the Academic and Administrative Plan, The Non-Academic Plan and the Eligible Part Time Employees Plan - are invested in a "mini mutual fund" format. All of these plans' assets are invested in a single Master Trust, which in turn is managed by the various investment counseling firms under different mandates. Each of the pension plans buys or sells units in the Master Trust monthly, depending on the net inflow or outflow for that plan. At the end of 1998, the Master Trust assets had a market value of $261.2 million.

The market value of the assets of the Academic and Administrative Pension Plan declined over the past year. Growth from income, capital gains, and contributions was more than offset by the impact of net withdrawals by members in excess of $17 million. This unusually high

amount of money transferred out of the fund was largely due to retirements and resignations under the Faculty Renewal/Voluntary Severance Plan.

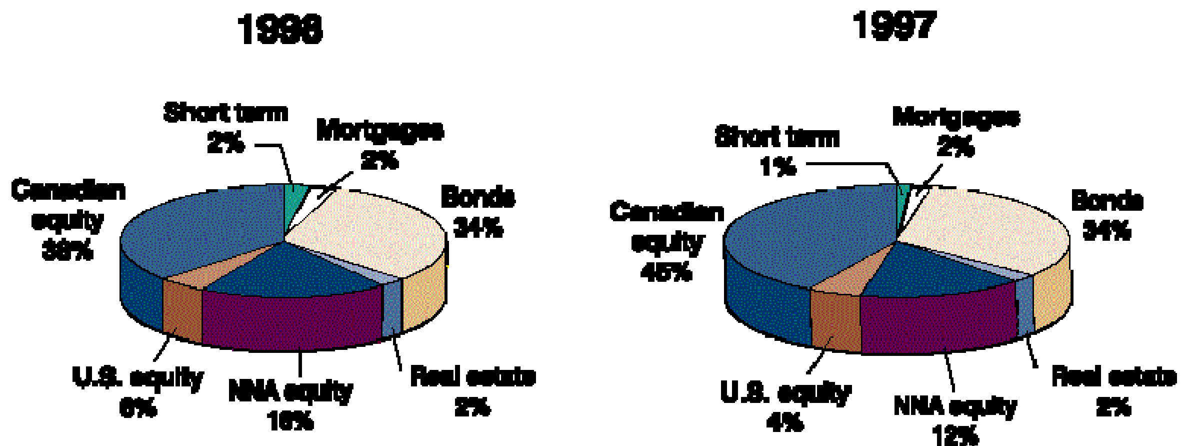
A listing of the assets of the Master Trust is available from Human Resources, on request. Alternatively, the list will be accessible via the Internet at http://www.cas.uregina.ca/~aabc/

	December 1998	December 1997
Academic Plan Market Value	$213,638,021	$216,839,827

Asset Mix Summary

The Master Trust maintained a relatively high equity weight over the past year, in part based on the balanced manager's (PH&N) preference for equities over bonds. In addition, the Joint Investment Committee allocated more funds to non-North American equities early in 1998, after seeing the book value of foreign investments fall well below the 20% maximum allowed under the *Income Tax Act*. The move was motivated by the objective to better diversify the Trust's assets and to make maximum use of the foreign investment limits. As noted earlier in the report, the Master Trust benefited from the additional international exposure, as markets outside of Canada generally provided stronger returns. The following graphs show the asset mix of the Master Trust as of December 1998 and 1997.

Distribution of Assets
(as a percentage of year-end market values)



Distribution of Assets by Manager

The investment management structure did not change during 1998. Phillips, Hager & North continue to manage a balanced mandate, and most of the Master Trust assets. The exposure to PH&N was reduced in the year because of transfers out of the academic and administrative plan and the increased investment in non-North American equities through Templeton. Baring also manages non-North American equities for the University. The other three specialty managers oversee real estate investments.

Allocation of Assets by Manager

	1998	1997
Phillips, Hager & North	84.1%	89.4%
Penreal Property Trust	1.4%	1.3%
Westpen Developments	0.4%	0.3%
Sun Life	0.5%	0.4%
Baring	3.9%	3.2%
Templeton	9.7%	5.4%

Detailed Analysis of Investment Returns

Canadian Stocks

The economic turmoil that began in Asia in 1997 sent commodity prices downward, impacting the Canadian equity market. The Toronto Stock Exchange 300 Index fell by 1.6% in 1998. The fund’s Canadian equity portfolio tracked ahead of this return with a -1.2% return. Relative to other funds, the University’s result hovered around median. Over four years, the fund’s 15.1% return on Canadian equities was also above the 13.6% index return and met the value-added objective of the investment policy. Relative to other funds, the four-year result was also approximately a median result.

U.S Stocks

The U.S. market continued to defy gravity in 1998, with the Standard & Poors 500 Index returning 38% in Canadian dollars. This is the third time in the past four years that the return on the S&P 500 index exceeded 30%. (In 1996, the index return was only 23.6%.) These very strong annual returns left the four-year result for the index at an annualized 33.5%. The fund’s U.S. equity portfolio did not keep up with the index in the year (23.1%) or the four-year period (27.1%). The surge in the index has been led by the very large companies and technology stocks, and has left most fund managers behind. In 1998, the S&P 500 index placed in 12th

percentile of funds in the CTUCS survey; i.e., only 12% of Canadian managers were able to outperform this U.S. index.

Non-North American Stocks

The last 12 months were strong for international markets, with European markets leading the way. Underlying the 28.8% EAFE Index return was a wide range of country returns. Finland led the way with 138% return in Canadian dollars, while Norway trailed other developed markets, losing 25%. Emerging markets, which are not represented in the EAFE Index, were hit hard in the year, as evidenced by the Emerging Market Free Index losing 22% of its value. The plan's objective, to at least match the EAFE Index return, was not met in 1998, as the foreign equity component of the Master Trust returned 17.0%. Each of the three managers investing offshore (Baring, Templeton, and PH&N) trailed the EAFE index return. Over the longer term, the results have been stronger, with Templeton and Baring adding value, and PH&N trailing the 12.1% index return slightly.

Real Estate

The real estate market continued to improve in the year, and the real estate index, RCPI™, provided its second consecutive year of double-digit returns (16.1% in 1998 and 18.9% in 1997). The fund's investments in real estate are made via Westpen Properties and Sunimco, which earned 12.3% and 10.6% respectively. The fund also has exposure to a real estate financing vehicle through Penreal Property Trust, which returned 10.8% over the past year. The combined rate of return on these three real estate investments was 11.0% in 1998.

Bonds

The fund earned 9.5% on its bond portfolio in 1998, outpacing the Scotia Capital Markets Universe Bond Index return of 9.2%. Over the past four years, the fund's return (13.0%) was also slightly ahead of the index return (12.8%). The value-added objective to achieve at least 105% of the index return was not met in the year and past four years. The slimmer value added for the fund's bond portfolio is reflective of the trend for many funds. The fund's 1998 bond result was slightly above median for the year, and close to the top one-third of funds over four years.

Mortgages

The fund's small exposure to mortgages produced a 9.1% return in 1998, well ahead of the Scotia Capital Markets Mortgage Index return of 7.0%. The performance objective was handily met in the latest year, as well as over the longer term. Over the past four years, the 10.0% return outpaced

the 7.6% index return. Relative to other funds, the University's four-year mortgage return placed in the top 25% of funds in the CTUCS survey.

1999 Interest Rate

The pension plan requires that interest be credited to members' account balances at the end of each calendar year. The rate of interest is equal to the annualized rate of return on the fund over the previous four years, net of expenses, less one-half of a percentage point. Therefore, the amount of interest added to each member's account on 31 December 1999 will equal 13.92% of that member's account balance at the end of 1998. Interest will be pro-rated for members who leave the employ of the University during 1999.

Amendments to the Plan

The plan was amended during 1998 to accommodate some clarifications requested by Revenue Canada. The Committee also asked the Actuary to prepare another amendment, in order to take advantage of a new Revenue Canada ruling about transfers out of a pension fund upon retirement or resignation. The ruling will have the effect of increasing some members' Maximum Transfer Values under Section 8517 of the *Income Tax Act*. For a member whose accumulated contributions exceed the Section 8517 limit, the new rules could result in a smaller amount of money being taken into taxable income when the member leaves the employ of the University.

Audited Statements

The Provincial Auditor audits the financial status of the University's pension assets each year. The Provincial Auditor provided an unqualified opinion of the 1998 financial statements of the Master Trust and the University's three pension plans. Any member who would like to receive a copy of the audited statements should contact Human Resources or consult the AABC web site.

Despite providing a clean audit opinion on the Academic and Administrative Pension Plan, the Provincial Auditor did raise two operational concerns: (a) timing of the approval of the budget for the administration of the pension plan; and (b) the way minutes of committee meetings are kept. The Committee is responding to those concerns promising to ensure that future budgets are approved before the beginning of each budget year, and by numbering committee meetings and ensuring that minutes are reviewed and approved promptly.

Pension and Benefits Review

The rationale, purpose and scope of the pension and benefits reviews have been explained in the two preceding annual reports. In a nutshell, the pension review has its origins in a desire to try to shield members from certain provisions of legislation that are perceived to limit their entitlements under the plan and their ability to save more money towards retirement. The benefits review was intended to determine how benefits plans at the University of Regina compare with those elsewhere.

The review of insurance plans was much more straightforward than the pension review. Ultimately, Gord Simle of William M. Mercer Limited presented a report to the Committee which, in turn, forwarded copies to the University and the Faculty Association. In December 1998, those two parties reached agreement on the establishment of an extended health care plan for Faculty Association members and their families and to extend dental insurance to the families of URFA members. These new plans take effect on 1 May 1999.

The review of the pension plan began in earnest in the fall of 1997, when William M. Mercer Limited was engaged to assist with the review process. Over the winter of 1997-98, the Committee considered several proposals put forward by Mercer, each of which carried some prospect of achieving the goals of the review. Early in 1998, the Committee began to focus exclusively on a creative approach that seemed to have the potential to address the concerns that had given rise to the review, while preserving the essence of the current plan. The Committee's enthusiasm for this novel design waned during the spring of 1998, however, as it became clear that federal and provincial pension regulators harbored serious reservations about the proposed new design. By August, the Committee had abandoned the Mercer proposal and began considering other options.

By October 1998, the Committee had narrowed its focus to just two plan designs. One option was to create a pure defined-contribution (DC) plan. A DC plan operates very much like a Registered Retirement Savings Plan; each member's contributions and those made by the plan sponsor in the name of that member are held in a separate account, and rise and fall with the markets until the member retires. At retirement, the member can use the accumulated funds to buy a life annuity, or transfer the funds into a tax-sheltered vehicle (e.g., a Retirement Income Fund) designed to generate income to support the member during retirement. The other favored option was to retain the current plan.

Changing to a DC plan would eliminate the transfer limits in Section 8517 of the *Income Tax Act* and provide members with more RRSP contribution room than they now have. However, the Committee felt that members would be reluctant to give up the current entitlement to a choice of a formula pension or a cash-out option, and decided to focus on reforming

the current plan. The fact that the current plan had been found wanting in some respects, and had therefore been the subject of a review, meant that it was essential that the Committee carefully review the provisions of the current plan before pronouncing an end to the pension review.

When the Board of Governors endorsed the pension review in 1997, it asked the Committee to take a number of specific factors into account as the review proceeded. One of the Board's concerns was the long-term sustainability of the plan. Under provincial pension legislation, the University is responsible for the payment of pensions earned under the current defined-benefit (DB) plan. If it should happen at some point that the plan were to fall into a deficit position, the Board would have to ensure that funds are available — perhaps from sources outside the plan — to ensure payment of pensions earned to that date. A concern about sustainability is a natural one for a plan sponsor.

To assess the sustainability of the current plan, the Actuary was asked to project the assets and liabilities of the plan into the future under two scenarios: (a) assuming no new members are allowed to join the plan; and (b) assuming that all future vacant positions are filled immediately. The results of this analysis were sobering. Under the closed-membership scenario, the financial health of the plan would remain strong, but the actuary's report suggested that the plan could be flirting with deficits if membership remained open. Another unnerving result of the study was an indication that the plan could find itself in a deficit position quite soon if market returns, inflation or salary patterns were to deviate adversely from the actuarial assumptions.

In light of this evidence, the Committee has recommended that the plan be closed to new members as of 31 December 1999, and that a pure defined-contribution plan be established on 1 January 2000 for all employees hired after that date.

Two questions arise naturally:

- **What effect would this change have on current members?** Current members would notice no difference if this change were made. They would continue to accrue service credit, build pension entitlements and retain the current transfer options. Indeed, closing the plan should make these benefits more secure than if the plan continues without amendment.
- **The pension fund has produced surpluses on a regular basis, so why should it suddenly be in danger of producing a deficit?** Arguably the fund is a victim of its own success. When the plan was established in 1965, a dollar's worth of contribution bought less than a dollar's worth of benefit. This was inherent in the design at that time, since the plan began with an unfunded liability because it promised full benefits in respect of members' service before 1965. As the years have passed, investment

performance has been good, and the fund has generated surpluses which led, in turn, to enhancements of members' entitlements. But, each enhancement carried a cost, to the point where the plan is now promising about $1.45 in benefits for each dollar contributed. Obviously, no company could stay in business for long if it sold items for a dollar that have a wholesale cost of $1.45, and it is no different for a pension plan.

The plan has been able to defy these economics because of market conditions in the 1990's: salaries (and therefore pension entitlements) and inflation have increased more slowly than the actuary assumed, while investment returns have been much, much higher than the actuarial assumption. Consequently, the plan has built up a surplus so large that one part of it has been hived off for use as a sort of bank to add 45 cents to every dollar contributed to the plan. However, recent improvements to the plan have considerably inhibited the plan's ability to earn surplus in future. In particular, the plan now credits interest to members' accounts at a rate just 0.5% less than the rate of return of the fund. This .5% "tax" generates very little surplus. The actuarial reserves in the plan will be a source of revenue only to the extent that the annual rate of return on the fund exceeds 7% (i.e., the yield assumed by the actuary) on the portion of the liability applicable to the retirees.

If the plan were to be left unamended, it would be necessary to have sufficient reserves to make sure that all new members can get the same 45-cent supplement to each dollar of their contributions as current members will get.

At this time (April 1999), the Committee's recommendation for changing the plan are under consideration, but have not been approved yet. The membership will be kept informed about the proposals and the process of implementing them, if approved.

Members of the Committee

- Norm Beirnes, Mathematics and Statistics (retired)
- Keith Johnson, Chemistry
- Gaynor Kybett, Computing Services
- Bob McCulloch, Associate Vice-President (Academic)
- Frank Proto, Member of Board of Governors
- Jim Tomkins, Acting Vice-President (Administration)
- Gary Tompkins, Economics

Recording Secretary

- Bonnie Dobni, Human Resources

Administrator

- Jim Tomkins, Acting Vice-President (Administration)

Actuary

- David Keet, Aon Consulting Group, Saskatoon

Pension Consultants

- James P. Marshall Inc., Regina

Primary Investment Managers

- Phillips, Hager and North Limited, Vancouver

Custodian

- CIBCMellon Trust, Calgary

Measurement Service

- Canadian Trust Universe Comparison Service (CTUCS)