WORKSAFEBC PENSION PLAN

FUNDING POLICY

November 24, 2021

WorkSafeBC Pension Plan

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A. PURPOSE OF FUNDING POLICY

The purpose of this funding policy is to provide a framework for the sound financial management of the Plan, and to guide decisions that must be made from time to time to maintain or restore a satisfactory funded status. The funding policy should set out a funding approach that is straightforward and predictable for the members and the employer.

This funding policy enables WorkSafeBC to be proactive in managing the financial status of the Plan, and will help to facilitate making any funding or benefit level decisions that may be required.

B. PLAN OVERVIEW

The WorkSafeBC Pension Plan (the "Plan") is a single employer defined benefit pension plan that provides pension and ancillary benefits for employees of the B.C. Workers' Compensation Board, known as WorkSafeBC.

The Plan is a key component of the overall total compensation package in recruiting and retaining skilled staff. Given that the provincial public sector is a key recruiting pool, the structure of the Plan and its portability with other plans in that sector make it critical to successful recruiting and retention of staff.

The Plan is a defined benefit plan where the pension payment is based on the number of years of Plan membership and the average of the highest five years of salary, independent of individual contributions to the Plan or the performance of the Plan's assets. The payments are made for the lifetime of the individual and may continue for the lifetime of the spouse based on the pension option chosen at the time of retirement.

The Plan comprises two[1] main accounts: the Basic Account and the Inflation Adjustment Account:

- The Basic Account is used to provide "basic" benefits including indexing up to the current date, but does not provide for future indexing.
- The Inflation Adjustment Account is used to provide future indexing on pension benefits on a non-guaranteed basis. The account is akin to a defined contribution account. The mechanics are such that the capitalized value of any indexing granted in a given year is transferred from the IAA to Basic at the time the indexing is granted.

[1] There is a third account, known as the Supplemental Benefits Account, which covers the payment of benefits in excess of those maximums allowed under the *ITA ;* since the Supplemental Benefit Account balance is maintained at zero, it is not considered in the funding policy.

All permanent full-time or part-time employees are automatically enrolled in the Plan. Plan members may retire at age 60 with an unreduced pension, provided they have two years of contributory service. The earliest retirement age is 55 with reduction, unless age and contributory service add to a total of 90 or more.

Effective January 1, 2012, employee contributions are made at the following rates:

(a) Basic Account: 5.5% of salary up to the YMPE and 7% of salary in excess of the YMPE (this is referred to as a contribution rate of 7% integrated);
(b) Inflation Adjustment Account: 1.0% of the employee's salary.

WorkSafeBC is required to contribute such amounts which, based on the recommendation of the actuary and subject to regulatory requirements, when combined with the employee contributions, are determined by WorkSafeBC to be necessary to provide for the benefits under the Plan. Actuarial surpluses may be used to reduce or eliminate contributions otherwise required.

Effective January 1, 2016 the employer contribution rate is:

(a) Basic Account: 5.5% of salary up to the YMPE and 7% of salary in excess of the YMPE (this is referred to as a contribution rate of 7% integrated);
(b) Inflation Adjustment Account: 1.0% of the employee's salary.

C. ROLES

Plan Sponsor - The Plan is sponsored by the Board of Directors (BOD) as a single employer, non-jointly trustee plan with the BOD bearing responsibility for the benefit promises of the Plan. No change can be made to the Plan language or investment policy without approval of the BOD.

Delegated Authority - The BOD has delegated day to day administrative responsibility to the Director, Total Rewards who interacts with required agencies, the Pension Committee, Plan agents and other entities. The Director will bring forward proposed changes to the Plan to the BOD for its review, approval, and adoption.

Pension Committee - Among other activities, the Pension Committee provides oversight on investments and makes investment decisions within the parameters established by the BOD, and makes recommendations to the BOD on changes to investment policy and Plan rules and language. Note that the Pension Committee does not have the authority to amend the investment policy or Plan Rules.

Administrative Agent - Contracted by the BOD to provide payment and management functions regarding the Plan and the employees covered by the Plan. Contract is tendered in keeping with Purchasing rules, and contract is negotiated by the Director, Total Rewards on behalf of the BOD. Ensures that the Plan and the Fund are administered prudently in accordance with applicable legislation and Plan language.

D. BELIEFS

This funding policy is developed with a foundation of two underlying beliefs, as follows:

Belief #1 - Intergenerational equity should be maintained such that, as much as possible, the contributions made in respect of each generation of members are self-sustaining for that generation. Generally, in order to maintain intergenerational equity, the long-term financial management of the Plan should reflect a balanced approach, and be neither:

a) too pessimistic about future Plan experience, with a result that benefits currently accruing to current members or being paid to Retirees are unnecessarily constrained, nor

b) too optimistic about future Plan experience, raising the risk of future Plan deficits or increases in Plan funding requirements.

Belief #2 - WorkSafeBC will continue to operate as the provider of workers' compensation benefits in BC for the foreseeable future. That being the case, the risk of a termination of the Plan is very small. Therefore, the primary focus for the Funding Policy is on the long-term management of the Plan. A secondary focus is the potential impact on the benefit security of Plan beneficiaries of the unlikely event of Plan termination in the short term. This means that, to the extent permitted by applicable legislation (summarized in Section F) and deemed reasonable by WorkSafeBC, funding decisions will not be based on short-term Plan termination scenarios where such decisions could impact significantly and adversely on long-term funding objectives or benefit provisions.

E. KEY RISKS

Key risks faced by the Plan are outlined below:

Investment: this is the risk that investment returns achieved by the Plan are less than the minimum returns required in the long term, such that contributions accumulated with investment returns are insufficient to support the benefits earned under the Plan.

Mortality/Longevity: the risk that the pattern of mortality actually experienced by Plan members differ from that assumed in a way that adversely impacts the funding of the Plan. The key risk here is that retired members live longer than they are assumed to in the actuarial valuation.

Demographic: this is the risk that Member demographics evolve in a way that adversely impacts the funding of the Plan. The key risks include:

- the average of the Active members accruing benefits increases, which increases the average cost to provide a set level of benefit;
- on average, members retire earlier than assumed in the actuarial valuation, which may increase costs where the early retirement discount applied is smaller, and hence more favourable to the member, than an actuarial neutral reduction;
- a significant number of members terminate their Plan membership prior to retirement and withdraw the lump sum value of the accrued benefit from the Plan, at a time(s) when the prescribed lump sum value is greater than the going concern value of the accrued benefit in the actuarial valuation.

Expense: this is the risk that administration expenses of the Plan are higher than expected, resulting in an increase in the normal actuarial cost (which contains an allowance for Plan administration expenses).

Inflation: this is the risk that actual inflation is higher than anticipated, and that the full indexing of pension benefits is not sustainable in the long term.

Asset/Liability Mismatch: In a matched portfolio, assets are chosen and invested to match the timing, duration and amount of the liability cashflows. Where there is a mismatch, there is a risk that interest rate shifts affect assets and liabilities differently, and that surplus decreases as a result (the converse is also true: surplus could increase as a result of a favourable interest shift). This risk can be more pronounced in the short-term under the solvency and expensing valuations.

Regulatory: this is the risk that legislative or regulatory requirements impact adversely on the funding requirements or other components of the Plan.

Political or Reputational: This is the risk the Plan is affected by political backlash or attack from outside. Political risk could include the risk that legislation changes are introduced that threaten or eliminate the Plan. Reputational risk could include the risk the Plan is perceived as overly generous to employees, and as a result becomes subject to political risk.

F. REGULATORY FRAMEWORK AND FUNDING REQUIREMENTS

The Plan must comply with requirements applying to:

- The *B.C. Pension Benefits Standards Act* (the "*PBSA*") which governs registered employment pension plans that have members in British Columbia. The *PBSA* includes restrictions on the investment activities of pension plans as well as minimum benefits, funding and solvency requirements.
- A registered pension plan under *The Income Tax Act (Canada)* (the "*ITA*"), which establishes maximum funding and benefits limitations that must be complied with under a registered pension plan.

Between the minimums dictated by the *PBSA* and the maximums per the *ITA*, there is some flexibility in determining contributions.

Under the *PBSA* and associated regulations, an actuarial valuation must be carried out at least every three years. The Plan rules and the Regulations associated with the *PBSA* permit the Board to have the valuation carried out at an earlier plan fiscal year-end.

The actuarial valuation must be performed on a:

***Going Concern Basis**,* for purposes of determining the funded status of the Plan and the ability of the Plan's assets and expected contribution in-flows to support expected benefit payouts, and the annual cost of benefits being earned; and

***Solvency Basis**,* for purposes of meeting minimum funding requirements and contribution adequacy under solvency funding rules.

The results of the regulatory (i.e. going concern and solvency) valuations include a balance sheet position (including the funded ratio for the going concern valuation and solvency ratio for the solvency valuation) and a measurement of the annual cost of benefits being earned and administration expenses incurred by the Plan (the "normal actuarial cost").

Specifically:

> ***"Funded Ratio"*** means the actuarial or smoothed value of assets divided by going concern accrued actuarial liability as disclosed in the most recent going concern valuation. The Provision for Adverse Deviation (PfAD) required under applicable Regulations is generally excluded from this calculation.
>
> ***"Solvency Ratio"*** is the solvency ratio disclosed in the most recent solvency valuation, calculated as the ratio of market value of assets less an allowance for wind-up expenses to the liability of the Plan calculated under a hypothetical wind-up scenario as required under applicable Regulations.
>
> ***"Minimum Funding Requirement"*** may comprise several components, including the normal actuarial cost plus any special payments required to amortize a going concern unfunded liability or maintain the PfAD required under applicable Regulations, or to amortize a solvency deficiency.

Under the current *PBSA* and associated Regulations, any shortfall of the going concern assets against the going concern liabilities plus the PfAD must be amortized over a period not exceeding 10 years. If there is a surplus on this measure, employer contributions may be reduced subject to these conditions:

- A surplus cushion equal to 5% of the sum of the Basic Account liability and the PfAD must be retained; and
- The remaining balance may be amortized over not less than 5 years; and
- There is no solvency deficit and the use of surplus to reduce contributions does not create a solvency deficit.

Under the current *PBSA* and associated Regulations, any shortfall of the solvency assets against 85% of the solvency liabilities must be paid over a period not exceeding 5 years. However, instead of making some or all of the required solvency deficiency payments, the *PBSA* allows an employer to use or continue to use a Letter of Credit to secure the solvency deficiency payments otherwise required for a particular year. The Letter of Credit must satisfy certain requirements set out in the *PBSA.* During the period that a Letter of Credit is utilized to secure solvency deficiency payments, contributions may not be less than the normal actuarial cost.

If the going concern funded ratio of the Plan (calculated on a fully indexed basis including both the Basic Account and the IAA and allowing for the PfAD) is greater than 125%, under the *ITA* and associated Regulations, employer contributions to the Plan may need to be reduced/eliminated.

In addition to the going concern and solvency valuations, the financial status of the Plan must be reviewed annually in accordance with the relevant accounting standards for the purpose of reporting in the audited financial statements of WorkSafeBC; this is referred to as the Expensing Basis Valuation. The Expensing Basis Valuation is carried out in accordance with IFRS requirements, as adopted in Canada. The Expensing Basis Valuation is not explicitly reflected in the funding policy, although the implications may be considered when making decisions within the funding policy framework.

G. FUNDING PHILOSOPHY AND OBJECTIVES

(a) Risk Sharing

In developing a pension plan funding policy philosophy, it is useful to consider the appropriate risk sharing approach. In general, for any particular risk factor, the entity that bears the risk of adverse experience should also reap the benefit of good experience.

Pension Plan Risk Sharing	
Pension Plan Risk	**Comment**
Investment	▪ Investment results can fluctuate dramatically; can be mitigated by maintaining a financial buffer (excess of assets over liabilities) in the Plan; if no buffer, adverse investment experience can cause significant variation in contribution requirements over time. ▪ Margin in valuation going concern assumptions provides buffer within going concern liabilities – this buffer gives long term protection but is difficult to draw on in the shorter term. The PfAD is the minimum buffer required by Regulations. ▪ Monitor via investment performance monitoring. ▪ Investment risk will be borne by WorkSafeBC, since WorkSafeBC has the ability to build up a buffer in the Basic Account and “ride out” periods of poor experience.

Mortality / Longevity	▪ Longevity experience tends to emerge over a long period of time. ▪ Can be managed through assumption-setting process in valuation and regular monitoring of the Plan's experience and the factors driving changes in life expectancies over time. ▪ Intergenerational equity suggests that normal actuarial cost reflect mortality assumption appropriate for current employees. ▪ Current employees participate in longevity risk via contributions towards normal actuarial cost, as this relates directly to the benefit each employee is accruing. Changes in normal actuarial cost arising from changes in mortality assumption will be shared with employees; exact sharing mechanism not specified; ▪ WSBC will take risk on shorter term mortality experience and risk on the impact that assumptions changes have on the accrued service liability.

Demographic	▪ May have both short term variation in demographic experience (i.e. cost of terminations if CV values high, rates of retirement in economic downturn) and long term trends (i.e. people generally retiring later, workforce older on average). ▪ Short-term impacts will emerge from valuation to valuation. ▪ Longer-term trends can be managed through assumption-setting process in valuation. ▪ As for longevity, employees will participate in long-term experience via contributions towards normal actuarial cost, while the employer takes the risk on shorter term demographic experience. ▪ Members will share in changes in normal actuarial cost arising from changes in other demographic assumptions; exact sharing mechanism not specified; WSBC will take risk on shorter term demographic experience and on the impact that assumptions changes have on accrued service liability.
Expense	▪ Plan administration expenses include items such as maintaining member records, member communication, preparation of financial statements, actuarial valuations, regulatory compliance, but exclude investment management expenses. ▪ Longer-term trends in expense levels are reflected in the expense allowance within the normal actuarial cost. ▪ Members will share in changes in normal actuarial cost arising from longer-term changes administration expenses; exact sharing mechanism not specified.
Inflation	▪ Inflation protection is provided via the IAA – indexing is granted to the extent it can be afforded. ▪ It is inherent in the structure of the Plan that employees participate in inflation risk.

Asset/Liability Mismatch	▪ Asset/liability mismatch risk arises in the Plan mainly in connection with the solvency valuation and solvency minimum funding requirements. ▪ Arises to a lesser extent in the going concern valuation. ▪ Monitor via triennial asset liability study. ▪ WorkSafeBC will bear this risk.
Regulatory or Political	▪ Regulatory and political risk is difficult to predict or manage. ▪ Low probability of adverse regulatory shift or political issues, but outcomes could be significantly different and likely adverse. ▪ These risks will be dealt with outside the Funding Policy when and if they emerge.

(b) Funding Philosophy

- Benefit security of the Basic Account is a primary objective;
- WorkSafeBC places a higher priority on contribution stability than on minimizing contributions;
- WorkSafeBC will bear the risk arising from experience gains and losses, and changes in economic assumptions (other than inflation);
- WorkSafeBC and the employees will share the risk arising from changes in demographic profile and demographic and administration expense assumptions that impact on normal actuarial cost; and
- The employees will bear the inflation risk, while WorkSafeBC will undertake to manage the Plan in such a way to support full indexing.

(c) Funding Objectives

The Plan is a key component of the overall compensation package provided by WorkSafeBC for its employees. The overall objective is to ensure the viability of the Plan over the long term.

(i) Basic Account

Benefit security is a key component of viability and is the primary funding objective for the Basic Account. The status of WorkSafeBC as a quasi-public sector entity enhances benefit security (in that there is a low likelihood that WorkSafeBC will cease to exist and a low probability of Plan termination). Benefit security can also be enhanced by investment quality, investment diversification, asset/liability matching, conservatism in actuarial methods and assumptions and retention of funding excesses.

Contribution stability is an important secondary objective for the Basic Account. This means that the capacity for the Plan to have assets in excess of liabilities to cover market fluctuations is important. Contribution stability can also be enhanced by asset smoothing, choice of actuarial cost method and assumptions, amortization of funding excesses and deficits and asset/liability matching.

(ii) IAA

In the context of the IAA, the objective is to provide a level of indexing that is sustainable in the very long term, without recourse to additional sources of funding.

Where there are sufficient funds in the IAA, full CPI indexing is provided; alternatively, if the funds in the IAA cannot provide full CPI indexing, then the amount of indexing is limited to the funds available.

The objective is to provide indexing from

(i) Current funds in IAA;
(ii) Future contributions to IAA at the rate of 1% WorkSafeBC and 1% employee;
(iii) Investment income on IAA assets; plus
(iv) Any excess investment income on assets backing the pensioner liabilities which is transferred from the Basic Account to the IAA;

without special payments or an increase in IAA contributions.

H. ACTUARIAL ASSUMPTIONS AND METHODS

(a) Going Concern Valuation

For the going concern valuation, the accrued benefit actuarial cost method shall be used to determine accrued actuarial liabilities; the accrued actuarial liability is equal to the actuarial present value of the portion of the benefits expected to be paid that is attributable to service prior to the valuation date, including assumed future salary growth.

The annual cost of benefits being earned (or normal actuarial cost) is calculated as the actuarial present values for benefits to be earned for service in the year following the valuation date.

The actuarial value of assets will be determined using a smoothing method, with investment gains or losses relative to a benchmark rate being smoothed over a period of not more than 5 years, consistent with accepted actuarial practice. Each year, the benchmark rate will be set equal to the real interest rate assumed in the most recent valuation plus CPI (i.e. the year-over-year change in the consumer price index).

A ceiling/floor will be applied to the smoothing mechanism, so that the smoothed value does not diverge by more than 10%, from the market value.

Actuarial assumptions for the going concern valuation are to be determined by the actuary as best estimate assumptions, modified to include margins or provision for adverse deviations that may be required by any relevant regulatory or professional body, and/or as required under this funding policy.

The assumption for future investment return on Plan assets (used to discount future liabilities) will:

- be determined using an economic building block approach and the Plan's investment policy; and
- may incorporate an explicit margin for adverse deviation.

Demographic and Plan expense assumptions will be based on Plan characteristics and experience, where practical, or on industry standard experience tables, with due regard to historical and economic trends.

(b) Sustainable Indexing Valuation

The Sustainable Indexing Valuation establishes the level of indexing that can be sustained in the long term. The Sustainable Indexing Valuation uses the going concern assumptions, with these modifications:

- Assets include both Basic Account and IAA;
- Liabilities are calculated based on a valuation of the total Plan i.e. including full indexing;
- Assumptions will be as for the Basic Account, except best estimate investment return and inflation assumptions are used (i.e. valuation margins are removed) and the PfAD is excluded; and
- Assets values are smoothed over a five year period. A ceiling/floor will be applied to the smoothing mechanism, so that the smoothed value does not diverge by more than 5%, from the market value.

(c) Solvency Valuation

Under the BC *PBSA,* a valuation of the hypothetical wind-up/solvency position of the Plan is required in order to (a) ensure minimum funding requirements are met, and (b) determine whether transfers of commuted values in respect of terminating or deceased members can be made in full, immediately, as these may be restricted by the solvency position of the Plan. The assumptions and method used in the solvency valuation are largely prescribed by applicable pension legislation.

I. FUNDING APPROACH

Changes in funding requirements or arrangements may arise from a filed actuarial valuation report, or changes in other circumstances affecting the Plan, including the overall compensation structure.

If there is a shortfall of going concern assets against the going concern liabilities plus the PfAD in the Basic Account, as indicated by the filed actuarial valuation report, WorkSafeBC will generally make the special payments required under the BC *PBSA,* in order to amortize the shortfall over the required period (currently no more than 10 years). Cost sharing of any such special payments with employees may be considered in unusual circumstances.

If the Basic Account Solvency Ratio is less than 85%, as indicated by the filed actuarial valuation report, WorkSafeBC may make the special solvency payments required under the BC *PBSA*, or may utilize a letter of credit to secure the solvency payments otherwise due as is permitted under the BC *PBSA*, or may utilize other avenues permitted under the BC *PBSA*.

Changes in the Basic Account normal actuarial cost, as indicated by the filed actuarial valuation report, arising from changes in mortality and other demographic and administration expense assumptions, or from shifts in the demographic profile of members, may be shared in part or full with employees.

Other changes in normal actuarial cost, as indicated by the filed actuarial valuation report, will generally be absorbed by WorkSafeBC. Cost sharing of these other changes in normal actuarial cost with employees may be considered in unusual circumstances.

Options for Utilizing Basic Account "Excess Assets"

The options for utilizing "surplus" in the Basic Account are subject to legislative requirements; in particular, a surplus cushion equal to 5% of the sum of the Basic Account going concern liability and PfAD must be retained and the remaining balance (the "Excess Assets ") may be amortized over not less than 5 years.

WorkSafeBC will assess the options for utilizing "Excess Assets" prudently, based on the benefit provisions established in the Plan and the objectives of this Funding Policy (benefit security and contribution stability in the Basic Account, and full indexing), and taking into account the long term best interests of the Plan and Plan members.

Specifically, the target minimum funded ratio for the Basic Account is that going concern assets are at least 110% of the going concern liabilities plus PfAD. The target minimum funded ratio for the Basic Account plus the IAA is 100% on the Sustainable Indexing Basis.

The major options in the event that the Plan has Excess Assets will be:

- Leave the Excess Assets in the Basic Account;
- Use the Excess Assets to reduce Basic Account contributions;
- Manage the Excess Assets through a combination of the above.

WorkSafeBC will generally utilize Excess Assets over not less than 15 years and not more than 25 years.

Where required, recommendations will be developed by Chief Financial Officer and/or Director, Total Rewards on behalf of BOD, feedback sought from the Pension Committee and then recommendations taken forward and approved by BOD.

J. FUNDING VOLATILITY FACTORS AND MANAGEMENT OF RISK

The Plan's liability structure, both current and projected, and related risks are taken into account, monitored and managed in the following main ways:

Statement of Investment Policies and Procedures: The status of the Plan's demographic and liability structure is taken into account in the Statement of Investment Policies and Procedures (the "SIP&P"). To enhance benefit security, the SIP&P specifies investment quality and diversification restrictions for the Plan assets. The Statement is monitored and approved or amended by the Pension Committee at least annually.

Asset/liability Studies: These studies project investment returns and the funded status of the Plan under multiple scenarios, involving assumptions for investment return and asset structure. The studies are used to develop probabilities of the funded status falling within certain ranges in future. These studies are undertaken for the Plan at least every 3 years. The following factors could trigger the study to be done earlier:

- Material change in the funded position of the Plan;
- Change in risk tolerance of WorkSafeBC;
- Significant change in assumptions used in the last study;
- Changes in capital markets;
- Results of liability projection;
- Amendments to the Pension Plan that would have material impact on either the assets or liabilities.

K. REVIEW AND MONITORING

This funding policy is the responsibility of the BOD and will be reviewed regularly and no less frequently than every three years by the BOD, and updated as required.

The BOD will seek input from the External Actuaries, Senior WorkSafeBC management, legislative requirements and any other sources deemed appropriate and will determine any changes to the policy to ensure that it reflects the needs of the organization and is compliant with applicable legislation.

The funding policy is not to be viewed in isolation. Rather, this funding policy, together with the Statement of Investment Policies and Procedures, and other monitoring initiatives described above, provides an organized framework for managing Plan financial risk.

L. COMMUNICATIONS

The intention is that the Funding Policy be a public document, available on the on the WSN Benefits Page under WorkSafeBC Pension Plan and on the WorkSafeBC Pension Plan website managed by the Pension Corporation along with other documentation related to the Plan and its operation.