# Workplace Safety and Insurance Board

Funding Sufficiency Plan

June 30, 2013

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# 1 Background

*An overview of governing legislation and Sufficiency Regulation*

The *Workplace Safety and Insurance Act*, *(Ontario) 1997* (the "WSIA" or the "Act") requires the Workplace Safety and Insurance Board (the "WSIB") to maintain the Insurance Fund such that the amount in the fund is sufficient to meet its obligations under the WSIA and to make payments to injured workers and their families when they come due. The WSIB charges premiums to Ontario employers from which to pay claims from injured workers.

Set forth below are the most pertinent excerpts from the Act with respect to funding and sufficiency:

- Section 96(2) of WSIA: *"The Board shall maintain the insurance fund (…) to pay for current benefits and to provide for future benefits under the insurance plan to workers employed by Schedule 1 employers and to the survivors of deceased workers (…)."*
- Section 96(3): *"Subject to the regulations, the Board shall maintain the insurance fund so that the amount of the fund is sufficient to allow the Board to meet its obligations under this Act to make payments under the insurance plan for current benefits as they become due and to provide for future benefits."*
- Section 96(5): *"The Board shall maintain the insurance fund so as not to burden unduly or unfairly any class of Schedule 1 employers with payments, in any year in respect of current benefits; or in future years in respect of future benefits."*

On January 1, 2013, *Ontario Regulation 141/12* "Insurance Fund," made under the Act came into force. In part, the regulation requires the WSIB to ensure the Insurance Fund meets the following Sufficiency Ratios by the following dates:

- 60 per cent on or before December 31, 2017
- 80 per cent on or before December 31, 2022
- 100 per cent on or before December 31, 2027

In addition, Section 96.1(1) of the Act requires the WSIB to develop and implement a plan to achieve sufficiency of the Insurance Fund based on the prescribed requirements (the "Sufficiency Plan"). *Ontario Regulation 141/12* sets out the information to be included in the Sufficiency Plan and requires that the plan be submitted to the Minister of Labour by June 30, 2013. This regulation came into force on January 1, 2013.

The WSIB Funding Policy, approved by the Board of Directors in June, 2013 outlines the principles it believes represent the tenets of a fair and transparent funding system. These principles are more fully described within the Funding Policy itself and include: collective liability, fair and reasonable allocation of aggregate costs, transparency, financial security, and compliance with the Act.

# 2 Purpose

*A description of the purpose of the Sufficiency Plan*

This Sufficiency Plan sets out the WSIB's plan toward attaining the required Sufficiency Ratios as mandated by *Ontario Regulation 141/12*, including: the definition, components and measurement of the Sufficiency Ratio; a summary of the more significant assumptions; and a discussion of significant risks and mitigation strategies.

## 3 Approach

*A summary of the approach to creating the Sufficiency Plan*

The WSIB has used conservative and prudent assumptions to ensure the WSIB has a high degree of confidence it will reach the funding requirements. Management has considered and assessed risks to the Sufficiency Plan and has robust mitigation strategies in place to monitor and manage those risks.

Premium rates are the WSIB's primary source of revenues. One of the guiding principles of the Sufficiency Plan is to provide employers with stability in rate setting and to guard against unexpected shocks to the rate system. The WSIB also must ensure the compensation system is sustainable and injured workers receive benefits and service.

To meet the Sufficiency Ratio requirements for 2017 through 2027, the WSIB will manage its investments to generate returns that meet the expected long-term rate of return, while prudently managing operations to ensure premium revenues absorb benefit costs, administrative and other expenses and provide an allocation toward the retirement of the Unfunded Liability, or UFL.

## 4 Sufficiency Ratio

*A description of the components and basis of measurement for the Sufficiency Ratio*

The Sufficiency Ratio was introduced through *Ontario Regulation 141/12*. The WSIB concluded that the objective of the Sufficiency Ratio should be: ***"To provide an objective measure to track achievement toward legislated and regulatory requirements and demonstrate sustainable funding."***

A standard measurement definition for the Sufficiency Ratio does not currently exist. Further, the WSIB is unique in having mandated Sufficiency Ratios within Regulation. The WSIB aims to have a Sufficiency Ratio measurement definition that will be consistent and demonstrates the integrity of reporting to all stakeholders. In so doing, the WSIB is guided by the Funding Policy. The Regulation requires assets to be measured, "in accordance with accepted accounting principles," and that liabilities are, "determined by the Board's actuary in an actuarial valuation."

The WSIB conducted significant research into the calculation of the Sufficiency Ratio for the purposes of *Ontario Regulation 141/12*, in addition to consulting with experts and performing a jurisdictional scan of other workers' compensation boards and relevant industries. Through this process, the WSIB has determined that a going concern methodology that values both assets and liabilities on a long-term, going concern basis would be reasonable and appropriate for the WSIB. This methodology would avoid rate fluctuations generated by financial market volatility.

*Ontario Regulation 141/12* currently does not permit the actuarial valuation of investment assets for the purposes of the Sufficiency Ratio. Accordingly, the WSIB has made a request for a regulation change to the Minister of Labour to allow the WSIB to value investments on a going concern basis for the purposes of calculating the Sufficiency Ratio.

For the purpose of the Sufficiency Ratio calculation, the WSIB proposes amortizing investment gains and losses that differ from the long-term assumed rate of return over a five-year period, thus moderating the effect of investment market volatility on financial results. The WSIB expects a long-term return on investments of 6.0%.

Amortizing returns over five years on a straight-line basis is consistent with guidance in the *Pension Benefits Act of Ontario* and is used by many large pension plans in Ontario. This approach takes into account the unique business requirements of Canadian workers' compensation systems, including the need for pricing stability (for employer premium rates) and benefit sustainability (for injured workers and their dependants). The amortization period of five years is considered an appropriate length of time to reduce the volatility of investment returns without deferring gains or losses unduly into future periods.

The WSIB's Sufficiency Statement will present its Sufficiency Ratio to stakeholders on a quarterly basis. The Sufficiency Statement will provide a reconciliation between the consolidated balance sheet for financial reporting purposes and the balances for Sufficiency Ratio purposes. Although our preferred basis incorporates a long-term expected rate of return in determining the asset values for Sufficiency Ratio purposes, we have adopted a mark-to-market basis consistent with the current Regulation. The detailed basis of measurement for the purposes of the Sufficiency Ratio under current Regulation is described below.

## Assets

Assets, for the purposes of the Sufficiency Ratio calculation, consist of the total consolidated assets of the WSIB less the interests in those assets of third parties, as represented by the balance of non-controlling interest and as presented in the consolidated financial statements of the WSIB. Investments on the consolidated financial statements of the WSIB are stated at market value in accordance with International Financial Reporting Standards ("IFRS").

## Liabilities

Liabilities, for the purposes of the Sufficiency Ratio calculation, are the total liabilities of the WSIB, adjusted for the items below:

### Discount rate for the obligation of the Employee Benefit Plans

In accordance with IFRS, the value of the obligation of the Employee Benefit Plans is based on market yields on high quality corporate bonds. For purposes of the calculation of the Sufficiency Ratio, the discount rate used is the same as the discount rate used for the Insurance Fund liabilities. This method is consistent with a calculation of the liability on a going concern basis as contrasted with the basis used under IFRS.

### Future changes in legislation, such as changes to benefits or services, accounting and actuarial calculation methodologies

Under IFRS, changes in accounting and actuarial standards are typically recorded in the year of change.

For purposes of the Sufficiency Ratio, any changes to legislation, regulation or accounting and/or actuarial standards that are minor will be recognized immediately. Changes that result in significant impacts to the Insurance Fund liability will be amortized over a reasonable period based on the size of their impact, the number of years to the next measurement date (2017, 2022 and 2027) and their relation to the regulated sufficiency requirements, such period not to exceed five years.

Based on the WSIB's Sufficiency Ratio methodology, outlined above, the Sufficiency Ratio as at December 31, 2012 was 56.9%, corresponding to a UFL of $13.1 billion on a sufficiency basis.

## 5 Risk Identification and Mitigation Strategies

*A discussion of the significant financial risks and mitigation strategies for those risks*

A discussion of the significant risk factors that affect the operations of the WSIB is included in the Management's Discussion and Analysis section of the 2012 Annual Report. The most significant risk factors that affect attainment of the legislated targets for the Sufficiency Ratio are noted below.

### Investments

The primary investment risk is that investment returns, taken together with a reasonable and sustainable level of premiums, are insufficient to meet the long-term obligations for which the Insurance Fund is established. This risk would be manifest in the failure to achieve a long-term return of 6% over a horizon of rolling ten to fifteen-year periods. The overarching risk mitigation tool for investment risk is through the diversification of investment return sources as provided for in the Statement of Investment Policies and Procedures, which is presented annually to the Board of Directors for its approval.

### Benefit liabilities

The WSIB, as the trust agency for administering the province's compensation system, must ensure there is adequate provision of funds to cover the cost of future payments on existing awards, both reported and unreported. The assurance is provided by ensuring benefit liabilities are calculated using sound actuarial practices and assumptions taking account of the long-term nature of the liabilities. Establishing an appropriate level of benefit liabilities is, therefore, an inherently uncertain process which presents a number of risks that could adversely affect the WSIB's comprehensive income and financial condition.

Risks are predominantly related to:

- Failure to accurately assess the future claims costs which may result in setting premium rates that are inadequate to cover costs and achieve sufficiency targets set by government
- Unforeseen changes in future patterns of claim continuance, incidence or inflation that could render the estimates inaccurate

The WSIB will mitigate these risks:

- By utilizing both proprietary and commercially available actuarial models and assessing historical loss development patterns to properly set long-term actuarial valuation assumptions
- By conducting adverse scenario testing on loss development patterns to ensure that premium rates can support such development should it occur
- With regular, ongoing reviews and re-evaluation of claims and assessing their impact on the estimate of the benefit liability
- By engaging external actuaries to review actuarial assumptions and methodologies in establishing benefit liabilities
- By reviewing actuarial related matters at regular meetings with the WSIB's Actuarial Advisory Committee and Chief Statistician

### Economic conditions and labour market changes

Given the WSIB's mandate to deliver a no-fault insurance plan, funded predominantly by premium revenue for operating capital, the WSIB is inherently subject to economic risks, including:

- Low or modest growth in Ontario's employment levels, especially in covered industries, which may result in not meeting premium revenue targets as well as limiting work transition opportunities

- The growing shift in the job market toward non-traditional jobs, such as knowledge work, generally supplied by not compulsorily covered firms which may adversely affect premium revenue
- The trend toward casual, part-time and temporary work that may result in return to work challenges and, therefore, higher claims costs
- A growing number of older workers in the workforce. If injured, they generally have a longer recovery time and a greater challenge with return to work

The WSIB will mitigate these risks by:

- Conducting economic forecasting to better project the level of future insurable earnings and the employment levels within the underlying industry sector
- Testing adverse economic growth scenarios to ensure that premium rates are set at a level that can support such changes
- Continuous monitoring and researching the job market for available, sustainable positions for injured workers ready to transition to the job market

### Regulatory, political and other influences

The mandate of the WSIB is subject to changing political and regulatory influences. Any reform or amendment to the WSIA could require the WSIB to make adjustments to its insurance fund liabilities. For example, changes in regulation can have an impact on the way the WSIB delivers services or the services themselves. This may require the dedication of WSIB resources to implement new systems or processes and/or address stakeholder concerns.

The WSIB will mitigate this risk by:

- Engaging with the Ministry of Labour to understand the intent of the changes and to consult on the potential impact to outcomes and capacity
- Consulting with the stakeholder community during the planning and implementation of the changes
- Ensuring that any changes to existing benefits and services are developed and implemented in a timely and seamless manner while ensuring they align with the WSIB's value propositions and organizational capabilities

## 6 Reporting Cycle

*An outline of reporting cadence and level of external assurance the WSIB will seek*

The WSIB will prepare a quarterly Sufficiency Statement that presents the Sufficiency Ratio and the measures underlying the ratio including reconciliation to its quarterly IFRS consolidated financial statements. This statement will describe the basis of preparation, level of assurance provided by the WSIB auditor and notes relating to the components of the calculation. Accompanying the quarterly statement will be a review of funding levels and risks, outlining significant changes occurring within the past quarter. The WSIB will obtain an audit opinion annually, consistent with IFRS consolidated financial statements. The WSIB operates with a calendar year-end of December 31.

## 7 Sufficiency Plan Renewal Process

*A description of how the WSIB will update the Sufficiency Plan*

On an annual basis, coincident with the annual consolidated financial report, the WSIB will prepare a companion document that provides additional information relating to the Sufficiency Plan. Specifically, the WSIB will report on:

- The impact (both quantitative and qualitative, if available) of any changes in assumptions or economic circumstance
- Mitigation strategy if changes lead to adverse impacts to the projected Sufficiency Ratios.

Schedule A outlines the major assumptions and projections underlying the Sufficiency Plan, as currently estimated. This schedule will be refreshed by the WSIB on an annual basis to reflect updated assumptions and projections.

## Schedule A: Summary of Significant Assumptions and Projections

*A summary of significant financial assumptions and projections of the Sufficiency Plan*

The WSIB has made the following significant assumptions in creating projections for this Sufficiency Plan:

1. Revenues
    - Premium rate increase of 0% in 2014, thereby maintaining an average premium rate of $2.46 per $100 of payroll
    - Insurable earnings are expected to grow at 3% annually (a combination of wage and employment growth)
    - Investment returns of 3.5% for 2013 to 2017 and 5.5% thereafter

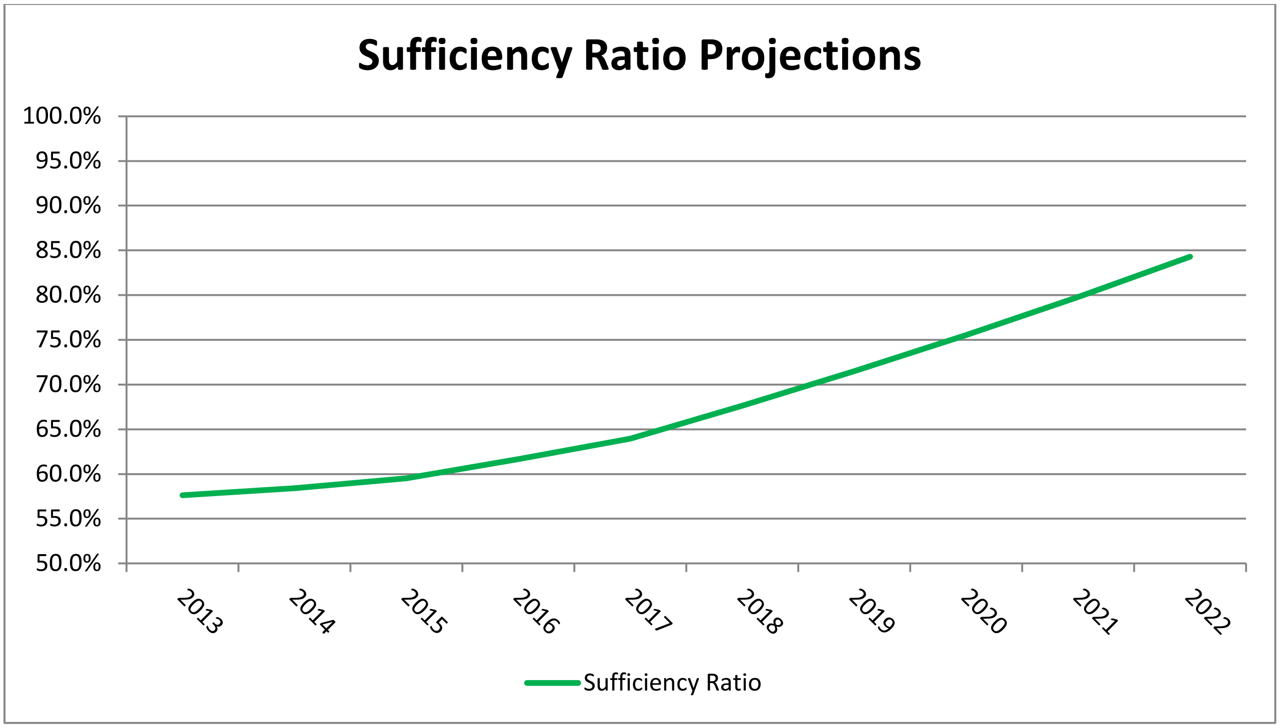
2. Claims
    - No change in benefit coverage or levels
    - Health care costs will grow at 4.5% per year
    - No improvement in duration of claims from 2012 actuarial valuation assumption
    - No improvement in Lost Time Injury claims
    - $1.10 per $100 of insurable earnings for New Claims Costs

3. Administration
    - Administration and other expenses will remain relatively stable until 2017 and then grow at 2% per year
    - CPI will grow by 2.5% annually

Using the above assumptions, the WSIB concluded it has a high probability of reaching 60% funding by 2017 and 80% by 2022. The WSIB has also made adverse assumptions to determine the margin for negative events in the economy. The projection results and stress testing indicate it is unlikely the WSIB would need significant additional premium increases in each of the three remaining years until the first Sufficiency Ratio requirement (2015 through 2017), even with adverse circumstances.

Set forth below are the WSIB's Sufficiency Ratio projections from 2013 through 2022. These projections are based on current expectations and various assumptions and analyses made by us in light of our experience and our perceptions of historical trends, current conditions and expected future developments and other factors we believe are appropriate in the circumstances. These projections involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated.

These factors may cause our actual performance and Sufficiency Ratios in future periods to differ materially from any estimates or projections of future performance or results expressed or implied by such projections. Projections do not take into account the effect that transactions or non-recurring or other special items announced or occurring after the projections are made have on our business. For example, they do not include the effect of asset impairments or other changes announced or occurring after the projections are made. The financial impact of such transactions and non-recurring and other special items can be complex and necessarily depends on the facts particular to each of them.




Based primarily on the assumptions outlined above, the WSIB projects the following Sufficiency Ratios as at December 31 of the respective year, highlighting the Sufficiency Ratio requirement dates set forth in *Ontario Regulation 141/12*:

| Year | Projected Sufficiency Ratio | Required Sufficiency Ratio |
|---|---|---|
| 2013 | 57.6% | |
| 2014 | 58.4% | |
| 2015 | 59.5% | |
| 2016 | 61.7% | |
| **2017** | **64.0%** | **60.0%** |
| 2018 | 67.6% | |
| 2019 | 71.5% | |
| 2020 | 75.5% | |
| 2021 | 79.8% | |
| **2022** | **84.3%** | **80.0%** |

## Appendix A: Proposed Basis of Measurement

*A description of the proposed basis of measurement for certain balances in the Sufficiency Ratio*

In order to ensure management used the most appropriate measures for the Sufficiency Ratio, the WSIB reviewed its balance sheet accounts to assess whether the current basis of measurement is appropriate. If the current basis were not appropriate, the WSIB would determine which basis of measurement would be appropriate.

The WSIB reports its financial results in accordance with IFRS. IFRS were designed to standardize financial reporting standards and principles of entities internationally and render financial statements more comparable across different geographies. IFRS are chiefly aimed at valuing an entity at a point in time, primarily for publicly traded corporations. Financial reporting under IFRS was not specifically designed for regulatory purposes and, accordingly, the WSIB undertook a review of its reporting under IFRS to determine whether certain balances should be measured using a different basis for sufficiency purposes. The areas the WSIB concluded require a different basis of measurement from IFRS are outlined in the table below.

| Balance Sheet Area | Primary Concern | Conclusion | Expected Benefits |
|---|---|---|---|
| Investments | Short-term market volatility | Amortize differences between expected and actual return over five years consistent with provincial pension regulations and ensure adjusted value does not deviate significantly from market<br><br>*Current regulation requires the valuation of assets at market value, which will not mitigate short-term market volatility. The WSIB has requested a regulation change to permit management's recommended basis of measurement | • Reduced volatility<br>• Improved premium rate stability<br>• *Current regulation requires the valuation of assets at market value, which will not mitigate short-term market volatility. The WSIB has requested a regulation change to permit management's recommended basis of measurement |

| Balance Sheet Area | Primary Concern | Conclusion | Expected Benefits |
|---|---|---|---|
| Insurance Benefits Liability | • Future IFRS revision to Insurance Contracts – market discount rate volatility<br>• Impact of mandated changes in benefit levels or in Actuarial and Accounting Standards - uncertainty in future periods | • Continue to use current going concern valuation method<br>• Recognize impacts to insurance liability immediately minor; otherwise amortize over a maximum five years, taking account of the number of years remaining until the next measurement date | • Reduced volatility<br>• Improved premium rate stability<br>• Consistency over long-term |
| Employee Benefit Plan | Short-term market discount rate volatility | Use going concern valuation method, consistent with insurance benefits liability and provincial pension regulations | • Reduced volatility<br>• Improved premium rate stability<br>• Consistency over long term |

The WSIB continues to believe its proposed basis of measurement outlined above is both reasonable and appropriate for the purposes of determining sufficiency. In the absence of regulation change, the WSIB will measure the Sufficiency Ratio in accordance with the Regulation and report investments at market values consistent with IFRS. The WSIB has requested an amendment of the Regulation from the Minister of Labour, which would permit the measurement of investments consistent with the proposed basis of measurement.