April 13, 2017

ONTARIO TEACHERS' PENSION PLAN FINANCIAL STATUS

What is the current funded status of the Ontario Teachers' Pension Plan (OTPP) and what are the implications for the government?

SUGGESTED RESPONSE

- **OTPP is jointly sponsored by the Ontario Teachers' Federation (OTF) and the Minister of Education (the Partners).**

- **The most recently filed actuarial valuation for the plan is as of January 1st, 2016.**

- **A preliminary valuation, as at January 1, 2017, showed an $11.5 billion surplus based on current plan provisions.**

    - **This includes a reduced level of inflation protection for service after 2009 and higher contribution rates.**

- **The surplus is a result of the Plan's strong investment performance in recent years.**

    - **OTPP earned 4.2% on its investments in 2016. The plan has about $175.6 billion in assets.**

- **The Partners will decide in the coming months whether to file the January 1, 2017 valuation with the Financial Services Commission of Ontario (FSCO) and how the surplus would be used.**

    - **The next required valuation is no later than January 1, 2019.**

2016 FINANCIAL RESULTS

The OTPP invests in over 50 countries. The return on investments was 7.2% in local currencies. However, volatility in global currencies last year had an impact on the short-term value of the OTPP's assets. After converting the return on those investments back into Canadian dollars (the currency in which pensions are paid), the OTPP's total-fund rate of return was 4.2 per cent.

OTPP has achieved an average return of 10% since its inception in 1990.

The value of OTPP assets increased from $171.4 billion at the end of 2015 to $175.6 billion at the end of 2016. Benefit payouts in 2016 were $5.7 billion.

The preliminary January 1, 2017 actuarial valuation showed an $11.5 billion surplus based on current plan provisions, which includes a reduced level of inflation protection for service after 2009 and higher contribution rates.

While this valuation need not be filed, they may choose to do so if the Partners decide to use a part of the surplus to, among other things, restore inflation protection and/or reduce contributions.

As a jointly sponsored pension plan (JSPP), OTPP is exempt from funding on a solvency basis.

BACKGROUND

OTPP reported its first funding deficit in 2005, after a period of small but steady funding surpluses.

The deficit situation was exacerbated by the 2008 financial turmoil as well as the demographic situation that is unique to the OTPP (i.e., a declining ratio of active teachers to retired teachers as well as continued mortality improvements).

To address the deficit, as well as the demographic issue, the Partners agreed in 2009 to make future inflation protection conditional on the financial health of the plan, known as conditional inflation protection (CIP). Amendments to the provision were made in 2012.

- Reducing the guaranteed level of inflation protection reduces the future liabilities of the plan, making it more affordable.

- For each year CIP is invoked, the government is required to make a "share the pain" payment to the fund in the amount equivalent to the amount of inflation protection forgone by retired teachers in that year, up to 50%. Any amount of inflation protection beyond 50% is not matched by the government.

The following is a summary of the CIP provision:

Service	Guaranteed Level of Inflation Protection	Current Inflation Protection Provided	Levels in 2018
Before 2010	100%	100%	100%
2010 to 2013	50% to 100%	90%	TBD
After 2013	No guarantee	90%	TBD

The following is a summary of the government's "share the pain" payments:

2010	2011	2012	2013	2014	2015	2016
$0.04 M	$0.22 M	$0.77 M	$1.05 M	$1.04 M	$1.12 M	$1.59 M

($ millions)

CIP has proven to be an effective tool for the Partners to manage deficits. With this tool, as well as the subsequent recovery of the financial markets, the OTPP has reported 4 consecutive funding surpluses since 2013.

- OTPP has achieved an average return of approximately 8% over the last 10 years, compared to the average benchmark return of 4.6% over the same period.

- The better than expected return has contributed to the recent funding surplus.

Future deficits, if any, could be addressed by reducing inflation protection to the minimum guaranteed level for service after 2009. Future surplus could be used to restore CIP and the government's "share the pain" payments would be reduced accordingly.

JSPP AGREEMENT

In March 2013, an agreement was reached between the government and the OTF to freeze contribution rates for a five-year period from 2013 to 2017, except in exceptional circumstances. If OTPP were to experience a new funding shortfall during the freeze period, then future benefits would be reduced, up to a limit, before increasing contributions. This is known as the JSPP Agreement.

The agreement expires on December 30, 2017.

Valuations must be filed at least every three years with the FSCO and CRA. Given that OTPP last filed a valuation as at January 1, 2016, the next required valuation will be the valuation as at January 1, 2019, after the freeze period.

Prepared by: Ingrid Tsang 416 327 1799 / Rob Pomykacz 416 327 0156
Broader Public Sector Pensions Branch
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Approved by: Leah Myers, ADM

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