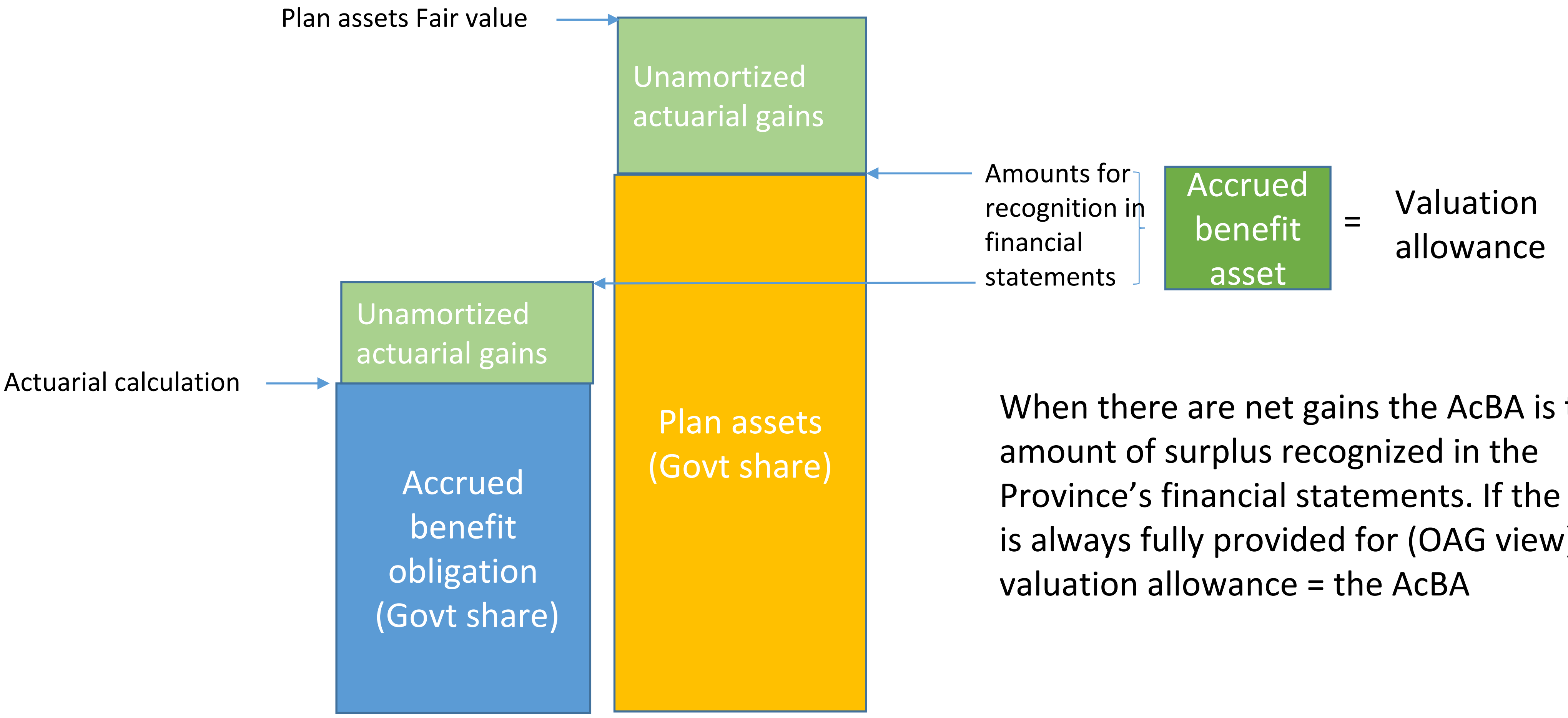
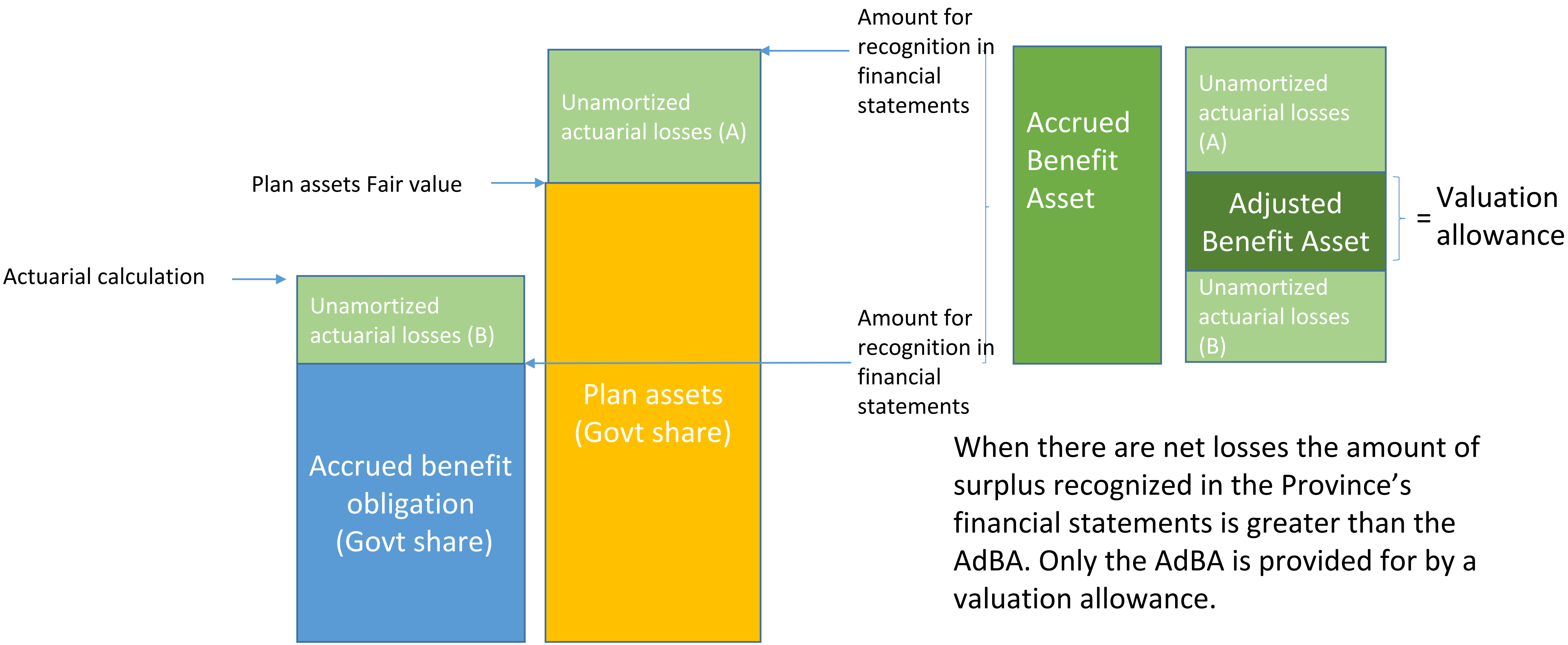
Impact of a Valuation Allowance on Pension Assets

An Accrued Benefit Asset (AcBA) occurs when there is a plan surplus, including the effect of net unamortized experience gains or losses. OTPP currently has net unamortized experience gains.
Actuarial (experience) gains can occur in respect to both plan assets as well as the pension obligation



When there are net gains the AcBA is the amount of surplus recognized in the Province's financial statements. If the AcBA is always fully provided for (OAG view) the valuation allowance = the AcBA

An Adjusted Benefit Asset (AdBA) is required when there are unamortized losses

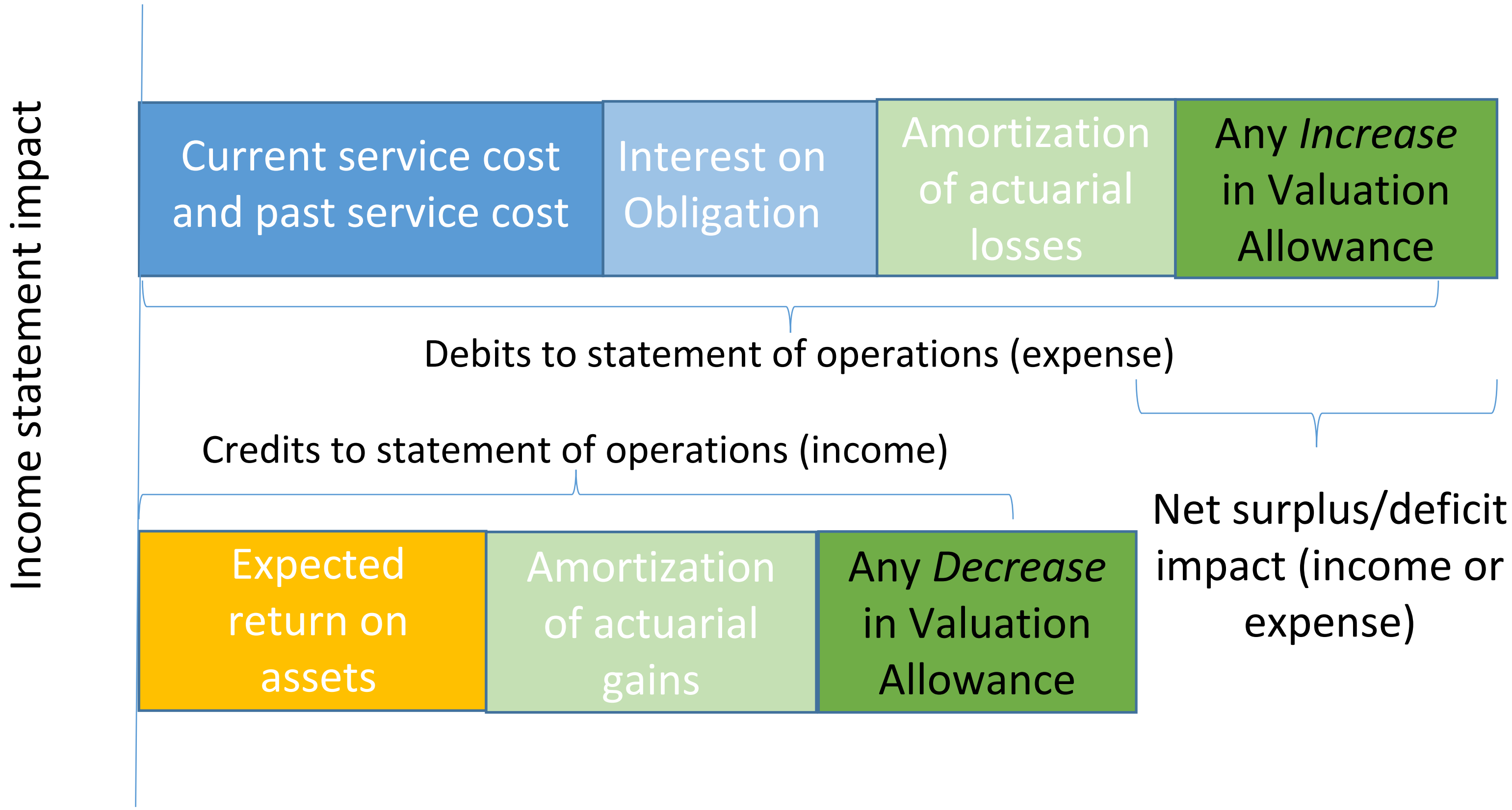


When there are net losses the amount of surplus recognized in the Province's financial statements is greater than the AdBA. Only the AdBA is provided for by a valuation allowance.

Components of Expense

The *change in* the valuation allowance flows directly through the statement of operations.

The change in valuation allowance = the change in the AcBA (or AdBA if applicable)



Changes in the Accrued Benefit Asset

Changes in the AcBA may occur for a number of reasons. Where changes result in an increase in the AcBA without expectation of future benefit, such changes would result in a change in the valuation allowance (VA) to effectively reduce the AcBA to zero. In this situation, the following impacts on the statement of operations would be noted [1]

Event or circumstance	Impact on ABA	Impact on VA	Impact on Fiscal position
Contributions in excess of current service cost – i.e. additional funding	Plan assets increase more than the ABO	VA increases to reduce ABA to zero	Fiscal position worsens with additional funding
2015-2016 example: Contributions of $1,812M exceeded other elements of pension expense by $1,514M	2015-2016 example: Additional contributions increase plan assets. AcBA increases by $1,514M	2015-2016 example: AcBA increase of $1,514M results in an increase to the VA of $1,514M	2015-2016 example: Deficit increases by $1,514M. The cash paid for contributions has not resulted in an asset and so is an expense, despite the funding position of the Province's share of the plan has been improved by the additional contributions.

[1] Impact of change, all other elements being held constant.

Changes in the Accrued Benefit Asset

Continuing from the previous slide, where valuation allowances are taken to effectively reduce the value of the AcBA to zero, in the year of a reduction in the value of the AcBA or AdBA, where an economic downturn occurs for example, the following impacts on the statement of operations would be noted [1]

Event or circumstance

Investment returns worse than expected e.g. economic downturn

Plan assets fair values significantly lower in one year.
Assuming no net amortized gains/losses in prior year this would create net *unamortized losses* as the use of market related values means the changes in plan assets are smoothed over 5 years.

Impact on AcBA/AdBA

The AcBA does not decrease significantly. The Adjusted Benefit Asset does.

The AcBA is based on the higher, smoothed value of plan assets and does not change significantly. However the actuarial losses are subtracted from the AcBA to calculate an AdBA, which is smaller than the AcBA.

Impact on VA

VA decreases – lower allowance than prior year required

Prior year allowance was based on AcBA (no net amortized actuarial losses). Current year is based on AdBA because there are unamortized actuarial losses. The AdBA is smaller than the AcBA because of the increase in unamortized losses. Therefore the VA is reduced correspondingly.

Impact on Fiscal Position

Fiscal position improves in an economic downturn

Fiscal position will be improved as a reduction in the VA results in a gain in the income statement in that year. The increased actuarial losses would only impact the statement of operations in future years.

A similar impact would have been noted in 2008 if the OAG's position was reflected in the financial statements for that year.

[1] Impact of change, all other elements being held constant.