

RE: New Question RE: MO Question: Pension Asset Value - 10:30 am deadline

From: "Fong, Pauline (TBS)" <pauline.fong@ontario.ca>
To: "Veinot, Cindy (TBS)" <cindy.veinot@ontario.ca>
Cc: "Hosick, Sarah (TBS)" <sarah.hosick@ontario.ca>
Date: Wed, 19 Oct 2016 09:42:44 -0400

Hi Cindy,

My edits are in green. If you have a chance please review and provide any further comments.

Pauline

From: Hosick, Sarah (TBS)
Sent: October-19-16 9:07 AM
To: Fong, Pauline (TBS)
Cc: Veinot, Cindy (TBS); Pomykacz, Rob (MOF)
Subject: RE: New Question RE: MO Question: Pension Asset Value - 10:30 am deadline

Hi Pauline,

Lots of interest on this one this morning...DMO has some questions/clarifications in red. Can we see what we can clarify for them by 10am? (sorry for the tight turnaround)

Let me know if any questions

Thanks
Sarah

The Province ~~s~~ (all of them?) follows Public Sector Accounting Standards (PSAS) in estimating their pension liabilities. The Public Sector Accounting Board (PSAB) of the Chartered Professional Accounts Canada (CPA) has the authority to set accounting standards for the public sector. PSAB standards represent generally accepted accounting principles (GAAP) for governments in Canada and are the primary source for public-sector accounting guidance in Canada. (who writes these standards, so we can reinforce legitimacy)

An accounting valuation is performed using Province's management's (do we need to say management or can we say: the Province's) best estimate of future events including expected inflation, salary escalation and investment return on plan assets. The purpose of an accounting valuation is to measure the pension benefits obligation at the end of the period or a point in time. The purpose is to attribute the cost of the pension benefit obligations to the period related to services that have been rendered over the employees' working life. (what does this previous sentence mean, thinking of a public audience) The discount rate used for both of these plans as of March 31, 2016 is 6.25%.

The Ontario Teachers' Pension Plan (OTPP) and Ontario Public Service Employee Union Pension Plan (OPSEUPP) discount rates of 4.8% and 5.55% are the discount rate used in their funding valuations. The funding basis valuation is performed to calculate the contributions required to secure the benefits promised. The results of the most recent funding valuations are available on the websites of the plans (<https://www.otpp.com/> for OTPP and <http://www.optrust.com/> for OPSEUPP). (do the plans have websites or the pension organizations - what can we call them) The most recent funding valuation for OTPP (as of January 1, 2016) reported a funding surplus of \$13.2 billion, and for OPSEUPP (as of

December 31, 2015) reported a funding surplus of \$8 million.

Because the purpose of a valuation for accounting versus funding is different (is this fact mentioned above? If not, should we mention and briefly say why – the fact is mentioned in the two paragraphs above), the discount rates and the methodologies used for the valuations differ.

From: Fong, Pauline (TBS)
Sent: October-19-16 8:45 AM
To: Hosick, Sarah (TBS)
Cc: Veinot, Cindy (TBS); Pomykacz, Rob (MOF)
Subject: RE: New Question RE: MO Question: Pension Asset Value - 10:30 am deadline

Hi Sarah,

The \$13.2 billion and \$8 million are using the discount rates of the plans itself and not the province's rates. The surplus for the plans are based on the plans funding valuation. We do not have the actuarial information to calculate the net pension assets for accounting purposes using the individual plan rates.

Pauline

From: Hosick, Sarah (TBS)
Sent: October-19-16 8:29 AM
To: Fong, Pauline (TBS)
Subject: Fw: New Question RE: MO Question: Pension Asset Value - 10:30 am deadline

Hi Pauline

Can you please take a quick look at the question below and confirm for me?

Sent from my BlackBerry 10 smartphone on the Rogers network.

From: Smith, Emilie (TBS) <Emilie.Smith@ontario.ca>
Sent: Wednesday, October 19, 2016 8:01 AM
To: Hosick, Sarah (TBS)
Subject: RE: New Question RE: MO Question: Pension Asset Value - 10:30 am deadline

Hi Sarah,

One quick question. Sebastian had originally asked for what the assets would look like using the pension fund discount rates. Can you confirm if the \$13.2 billion and \$8 million below are using the pension discount rates and not the governments?

Many thanks,
Emilie

From: Hosick, Sarah (TBS)
Sent: October-18-16 3:37 PM
To: Makrigeorgos, Niki (TBS); Smith, Emilie (TBS)
Cc: @TBS-L-Issues and Media; Lin, Kim (TBS); Srimurugan, Liya (TBS); Bissoon, Nadine (TBS)
Subject: RE: New Question RE: MO Question: Pension Asset Value - 10:30 am deadline

Hi Emilie,

Please see below for the response prepared by OPCD:

Provinces follows Public Sector Accounting Standards (PSAS) in estimating their pension liabilities. An accounting valuation is performed using management's best estimate of future events including expected inflation, salary escalation and investment return on plan assets. The purpose of an accounting valuation is to measure the pension benefits obligation at the end of the period or a point in time. The purpose is to attribute the cost of the pension benefit obligations to the period related to services that have been rendered. The discount rate used for both of these plans as of March 31, 2016 is 6.25%.

The OTPP and OSPEUPP discount rates of 4.8% and 5.55% are the discount rate used in their funding valuations. The funding basis valuation is performed to calculate the contributions required to secure the benefits promised. The results of the most recent funding valuations are available on the websites of the plans. The most recent funding valuation for OTPP (as of January 1, 2016) reported a funding surplus of \$13.2 billion, and for OPSEUPP (as of December 31, 2015) reported a funding surplus of \$8 million.

Because the purpose of a valuation for accounting versus funding is different, the discount rates and the methodologies used for the valuations differ.

Thanks,
Sarah

From: Makrigeorgos, Niki (TBS)
Sent: October-18-16 11:22 AM
To: Smith, Emilie (TBS); Hosick, Sarah (TBS)
Cc: @TBS-L-Issues and Media; Lin, Kim (TBS); Srimurugan, Liya (TBS); Bissoon, Nadine (TBS)
Subject: RE: New Question RE: MO Question: Pension Asset Value - 10:30 am deadline

Hi Emilie

I have confirmed with program area that TCSB is not able to answer any of these - this is an OPCD lead

Thanks

From: Smith, Emilie (TBS)
Sent: October-18-16 11:16 AM
To: Makrigeorgos, Niki (TBS); Hosick, Sarah (TBS)
Cc: @TBS-L-Issues and Media; Lin, Kim (TBS); Srimurugan, Liya (TBS); Bissoon, Nadine (TBS)
Subject: RE: New Question RE: MO Question: Pension Asset Value - 10:30 am deadline

Thanks Niki!

From: Makrigeorgos, Niki (TBS)
Sent: October-18-16 11:15 AM
To: Smith, Emilie (TBS); Hosick, Sarah (TBS)
Cc: @TBS-L-Issues and Media; Lin, Kim (TBS); Srimurugan, Liya (TBS); Bissoon, Nadine (TBS)
Subject: RE: New Question RE: MO Question: Pension Asset Value - 10:30 am deadline

Hi Emilie

Working with program area on getting you a response to the 6.25% discount rate

Thanks

From: Smith, Emilie (TBS)

Sent: October-18-16 10:34 AM
To: Hosick, Sarah (TBS); Makrigeorgos, Niki (TBS)
Cc: @TBS-L-Issues and Media
Subject: RE: New Question RE: MO Question: Pension Asset Value - 10:30 am deadline

Hi Sarah and Niki,

Checking in on this request. I know there's a lot of requests this morning and on top of TB/MBC submission and the Deputy briefing this morning.

Many thanks,
Emilie

From: Smith, Emilie (TBS)
Sent: October-18-16 9:47 AM
To: Hosick, Sarah (TBS); Makrigeorgos, Niki (TBS)
Cc: @TBS-L-Issues and Media
Subject: New Question RE: MO Question: Pension Asset Value - 10:30 am deadline
Importance: High

Hi Sarah and Niki,

I've confirmed with the MO that the response to the questions below will come tomorrow morning. In the meantime, they've asked for one line on the justification of the governments use of the 6.25% discount rate for **10:30am**.

Apologies for the rush and multiple requests this morning.

-Emilie

From: Hosick, Sarah (TBS)
Sent: October-18-16 9:19 AM
To: Smith, Emilie (TBS); Makrigeorgos, Niki (TBS)
Cc: @TBS-L-Issues and Media
Subject: RE: MO Question: Pension Asset Value - 10 am deadline

Same on our end – we don't have this information offhand. Program area here will see if this is something we can help calculate or shed light on today.

Thanks,
Sarah

From: Smith, Emilie (TBS)
Sent: October-18-16 9:16 AM
To: Makrigeorgos, Niki (TBS); Hosick, Sarah (TBS)
Cc: @TBS-L-Issues and Media
Subject: RE: MO Question: Pension Asset Value - 10 am deadline

Thanks Niki! I'll let the MO know to expect the response tomorrow morning.

From: Makrigeorgos, Niki (TBS)
Sent: October-18-16 9:15 AM
To: Smith, Emilie (TBS); Hosick, Sarah (TBS)
Cc: @TBS-L-Issues and Media
Subject: RE: MO Question: Pension Asset Value - 10 am deadline

Hi Emilie

We need more time with this. Program area is working on a TB/MBC submission and prepping for a DM briefing this morning

From: Smith, Emilie (TBS)
Sent: October-18-16 9:08 AM
To: Hosick, Sarah (TBS); Makrigeorgos, Niki (TBS)
Cc: @TBS-L-Issues and Media
Subject: RE: MO Question: Pension Asset Value - 10 am deadline

Hi Sarah and Niki,

Checking in to see if it's possible to provide this information this morning to the MO?

Many thanks,
Emilie

From: Smith, Emilie (TBS)
Sent: October-18-16 8:11 AM
To: Hosick, Sarah (TBS); Makrigeorgos, Niki (TBS)
Cc: @TBS-L-Issues and Media
Subject: RE: MO Question: Pension Asset Value - 10 am deadline
Importance: High

Looping Niki in for ERD.

From: Smith, Emilie (TBS)
Sent: October-18-16 7:54 AM
To: Hosick, Sarah (TBS)
Cc: @TBS-L-Issues and Media
Subject: MO Question: Pension Asset Value - 10 am deadline
Importance: High

Hi Sarah,

The MO has a question from the two articles below that appeared in the clips this morning. I've included both articles below. They would like to confirm the rates that we discount our pension liabilities and the rates OTPP and OPSEUPP plans discount themselves. They would also like to know what the pension assets would look like using the pension fund discount rate. I've included the full question from the MO below as well. They've asked if this is readily available they would like it by **10am today**, if this is something that would need to be calculated, tomorrow at 10am would be great.

Can you please confirm if you're able to provide this information this morning or if it will need to be calculated.

Many thanks,
Emilie

They report that we discount our pension liabilities at 6.25%, and that the OTPP and OPSEUPP plans respectively discount themselves at 4.8% and 5.55%. At least in OTPP's case, I was made to understand that even using the pension plan's own discount rate, the plan was still overfunded.

If that's the case, it somewhat renders much of the hypothetical argument presented moot, and (if it continues) brings us back into a space where we are discussing what discount rate to use, and not if we can consider future contribution holidays as an asset for jointly sponsored pension plans.

Would we be able to find out what the assets look like using the pension fund discount rates?

If the asset value as reported by OTPP and OPSEUPP is something they have on hand readily, it

would be great for Question Period today (10:00)

If the number isn't on hand, and it needs to be calculated, then tomorrow morning for 10:00 would be great.

Wynne government is missing the big picture on Ontario finances (Waterloo Record)

Waterloo Region Record

Tue Oct 18 2016

Page: A6

Section: EDITORIAL

Byline: Ben Eisen and Charles Lammam

The Ontario government is reportedly in a spat with the province's auditor general about the size of last year's deficit. The auditor general pegs the shortfall at \$5 billion, whereas the government, using a different accounting method, says it's somewhat lower at \$3.5 billion.

It's not surprising the Wynne government is willing to go to the mat to defend its estimate of last year's budget deficit. As we approach the next election, a big part of the government's PR strategy is focused on celebrating an expected return to a balanced budget. So Premier Wynne's team has a big incentive to push back against dissenting views.

The source of the dispute hinges on the government's desire to use a surplus from public-sector pension plans to cover its operating deficit. The auditor general disagrees.

We hope that proper accounting practices prevail in the end. But in bickering with the auditor general over the precise size of last year's operating deficit, and with its fixation on being able to announce a balanced operating budget next year, the provincial government completely misses the bigger picture. Regardless of the exact size of the government's operating budget balance this year or next, provincial finances are in bad shape and the Wynne government must develop a credible plan to repair them.

To understand why, we first need to distinguish between a government's "deficit" and its "debt." A government's deficit is the difference between its annual revenues and spending (including debt service payments). A government's debt, meanwhile, represents all the outstanding financial liabilities it has accumulated throughout its history.

Even if the government is finally able to claim no deficit next year, the mountain of debt accumulated over the past nine years will still be there. Just how big is this mountain? Since 2007, Ontario has seen its net debt (a measure of debt that adjusts for financial assets) approximately double, climbing from \$157 billion to \$308 billion. That's about \$21,000 per Ontarian. Servicing all of this debt will burden Ontarian taxpayers for many years.

A balanced operating budget next year won't address this debt burden. In fact, the government's own Financial Accountability Office (FAO) projects that provincial debt will continue to climb in years ahead, reaching \$350 billion by 2020/21.

How can this be the case? Two reasons.

First, Ontario will accumulate new debt because the Wynne government plans to ramp up capital spending on things such as roads and bridges, which will be financed by more debt. The province can add debt, despite having a balanced operating budget, because its capital and operating budgets are accounted for separately. Indeed, the operating budget can be balanced at the same time the capital budget is in deficit.

Second, the balanced operating budget in 2017/18 may be tenuous. According to the FAO, the government has not done enough to bring spending sustainably in line with revenues. Without policy reform, the province will likely slip back into operating deficits after just one year of a balanced budget.

The Wynne government is nonetheless determined to spin the projected balance budget for 2017/18 as evidence of prudent management of public finances and justification to further loosen the purse strings, especially to provide yet even higher pay to public-sector employees (again, just in time for the election). It's a politically appealing narrative, but it doesn't withstand scrutiny. The Wynne government has no plan to pay down the debt, and actually plans to pile on more. The work of repairing Ontario's battered finances remains undone.

Ben Eisen and Charles Lammam are analysts with the Fraser Institute (www.fraserinstitute.org).

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Memo to Ontario Taxpayers - Auditor General's Objections to Ontario's Pension Accounting are the Tip of a Fiscal Iceberg (C.D. Howe Institute)

From: Bill Robson and Alexandre Laurin

To: Concerned Ontarians

Date: October 17, 2016

Re: Memo to Ontario Taxpayers - Auditor General's Objections to Ontario's Pension Accounting are the Tip of a Fiscal Iceberg

The release of Ontario's public accounts for the 2015/16 fiscal year in early October featured an unusual tussle between the government and the provincial Auditor General (AG). The AG's unwillingness to approve Ontario's treatment of public sector pensions in its consolidated financial statements prompted the government to issue unaudited statements – an unprecedented move. While Ontario released audited statements shortly afterwards, with a qualified opinion from the AG, issues at stake in this dispute are larger – and more problematic for Ontario taxpayers – than they look.

The dispute over the public accounts centres on the government's treatment of the Ontario Teachers Pension Plan (OTPP) and the Ontario Public Service Employees' Union Pension Plan (OPSEUPP) in its financial statements. The province has been netting pension assets against pension liabilities related to these plans, reducing the reported provincial debt and improving its annual results, lately reducing the provincial deficit. The provincial AG, Bonnie Lysyk, [objects to that treatment](#).

The main issue highlighted in [Ms. Lysyk's statement on the dispute](#) is that the province has no certain access to any funding surplus that may arise in these pension plans, which are jointly-governed risk-sharing plans. For taxpayers to benefit from a surplus, the partners governing these plans would have to agree to reduce government contributions. The fact that OTPP is using some of its recorded surplus to [partially restore inflation increases](#) for accruing benefits supports the AG's interpretation.

Ms. Lysyk has argued for a valuation allowance annihilating the effect of these surpluses on the balance sheet. And in the documents it has now released, the province did include an allowance related to these plans – increasing the province's reported debt by \$10.7 billion, and worsening its annual deficit from \$3.5 to \$5.0 billion. If the province were to restate previous years' results similarly, it would satisfy Ms. Lysyk's objections. But problems with Ontario's pension accounting are much bigger than this.

The AG's statement does not mention it explicitly, but the province gets these positive pension-related values by understating the value of its pension promises. Private-sector sponsors of defined-benefit pension plans must value their liabilities by discounting future payments at rates reflecting the debt-like nature of these obligations: the yields on bonds of appropriate credit quality. However, Ontario, like governments elsewhere, discounts future pension promises using generous assumed rates of return on assets. This practice understates [public-sector pension benefits](#) and the [costs of employee compensation](#).

Ontario discounts OTPP and OPSEUPP liabilities at 6.25 percent for its financial statements. While not as high as the discount rate used by bankrupt Detroit, it is far above Ontario Savings Bonds – [currently 2.2 percent](#). And – a particular sticking point for the AG – it is above the rates the plans themselves use – 4.8 and 5.55 percent. Using a more appropriate discount rate would show not pension surpluses, but deficits – and likely big ones.

Ms. Lysyk has brought part of the problem with Ontario's pension accounting to light. But taxpayers in

Ontario, like their fellows elsewhere in Canada, are still exposed to risks much larger than their governments admit.

Alexandre Laurin is Director of Research, and Bill Robson is the President and CEO of the C.D. Howe Institute.

Emilie Smith

Senior Corporate Issues Management Analyst
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