Statement of Facts and Assumptions

The (Ontario Teachers') pension plan is jointly sponsored by the Ontario government, through the Minister of Education, and the executive of the Ontario Teachers' Federation (OTF). The OTF represents teachers, while the government represents employers.

OTF and the government are equally responsible for ensuring the pension plan has enough money to meet its long-term pension obligations. In addition, they appoint experienced, professional experts to the pension plan's Board.

Through a six-member Partners' Committee, the sponsors jointly:

- Set benefit levels
- Establish the contribution rate paid by working teachers (which is matched by the Ontario government and other designated employers)
- Decide how to address funding shortfalls or use surplus funds when they arise

(Source: OTPP.com)

The governing and other documents that are relevant to an accounting analysis are as follows:

- Teachers' Pension Act (TPA)
- Partners' Agreement
- Funding Management Policy (FMP)

The following facts and assumptions have been accepted without verification or further analysis:

- The plan meets the definition of a joint benefit plan under S. 3250 of the Public Sector Handbook and is appropriately accounted for as such.
- The actuarial and other assumptions that factored into the valuation used for accounting purposes are appropriate and meet the requirements of S. 3250.

Relevant Extracts from the TPA

Section 5 (1.1) of the TPA states that the total amount of contributions payable by the Minister of Education and the employers who contribute under the pension plan in respect of any year shall not exceed the amount of contributions payable by or on behalf of active plan members in respect of credited service for that year. The only instance where contributions would not be equal would include the government's payments in connection with forgone inflation adjustments (which is often referred to as "share the pain" payments) and the additional contributions related to the 2008 filing agreement (1.1%) (Section 5 (8)).

Section 10 of the TPA provides that the Minister of Education and the executive of OTF may enter into an agreement that provides for, among other things, the joint management of the Plan and the sharing of entitlement to gains or surplus under the plan and of liability for deficiencies in the pension fund.

Pursuant to Section 10 of the TPA, the Minister of Education and the OTF (collectively the Partners) have entered into an agreement for the management of the Plan (Partners' Agreement), to which is appended a Funding Management Policy (FMP) that is deemed to form part of the agreement.[1] The FMP provides for the funding of the Plan and how deficits and surpluses will be addressed.

Actuarial Valuation of the OTPP for accounting and funding purposes

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[1] Partners' Agreement, section 110.

The following is a summary of the components of the plan and the Province's calculation of its share of the plan as of March 31, 2016 on an accounting valuation basis.

(all figures in $B)	Total plan	50% Share of the Plan
Market related value of assets	157.0	78.5
Value of obligation	116.4	58.2
Surplus (deficit)	40.6	20.3
Unamortized (gains) losses	(18.0)	(9.0)
Adjustment for March 31, 2016	(1.8)	(0.9)
Asset (liability) position	20.8	10.4
Specific Government adjustment		(0.3)
Final asset (liability) position on balance sheet		10.1

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Funding: The Plan's most recent preliminary funding valuation reported a surplus of $13.2 billion as at January 1, 2016.

Relevant Extracts from the Partners' Agreement

The Partners' Agreement is between the Province of Ontario and the OTF it sets out the formal relationship between the partners in sponsoring the OTPP. Paragraph 8 of the Partnership Agreement states that the partners will be responsible for designing the plan structure, setting the benefits of the plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, making changes to the plan, this agreement or other plan documents, deciding whether or not to file a valuation more frequently than required by the *Pension Benefits Act,* appointing the OTTP Board, and defining the role of the Board.

The Partners' Agreement requires that when changes to the plan are required that the Partners negotiate how those changes are made in good faith (Paragraph 74).

Paragraph 75 of the Partners' Agreement requires the Partners to advise the Board of OTPP of what changes affecting benefits and contribution rates they are proposing so that the Board can provide cost estimates and comments on the administrative impact of the changes to both partners as soon as possible.

If the partners cannot agree on the changes required to the plan, a mediator is appointed to assist the Partners in coming up with an agreement. The mediator is responsible for submitting a report to the partners on his or her views on the positions of the partners and provide a recommendation to the Partners. If the partners do not accept the mediator's report, the arbitration process will begin and an arbitration board will be appointed. The board will consist of 3 people, with each partner selecting one representative and two appointees will select the final member who is an umpire. Paragraph 94 of the Partners' Agreement indicates that the report created by the arbitration board will be implemented. Paragraph 92 sets some parameters for the mediation, including part (c), which sets out that the contributions from the Minister and employers be equal to those of the members.

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In addition to the clauses identified above, the Partners' Aagreement has an appendix called the Funding Management Policy which sets out the Partners' responsibilities in making funding decisions and surplus allocation regarding the plan.

Relevant Extracts from the FMP

The FMP is an appendix to the Partners' Agreement that speaks to how the plan should be funded by both parties. The protocol for the use of surplus under the OTPP is detailed in the FMP adopted by the Ontario Government and OTF as sponsors of the OTPP.

The FMP sets out a complex series of considerations surrounding funding management and the use of any excess of assets over liabilities. The FMP sets out a number of "funding zones", depending on the level of funding in the plan. The following three are most relevant to addressing surpluses:

i) Restoration zone (Article 3 of the FMP) allows for surplus to be utilized to "restore" foregone indexation and then to either increase benefits to the "run-rate benefit" level (i.e., the long-term target level) or to lower contributions to the basic target rate (or a combination of these two options) (Section 3.06(e)).

ii) Temporary improvement zone (Article 4 of the FMP) is the zone where contributions can be temporarily reduced, a surplus distribution can be made on a temporary basis and/or benefits can be temporarily improved (as long as it does not create a long term cost). Section 4.05 of the FMP provides that in such a scenario, the parties may reduce current contributions, provide temporary surplus distributions or provide a temporary benefit improvement.

iii) Permanent improvement zone is where the plan is essentially fully funded and has the funding security desired to support permanent changes. Article V (Permanent Improvements) of the FMP provides for permanent actions that can be taken when Plan assets exceed current liabilities by more than 10% of current liabilities. Section 5.05 provides for actions that can be taken in respect of the amount that assets exceed current liabilities plus the 10% margin noted previously. Such actions can include changes to current benefits, current contributions, or both.

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The ability to reduce contributions or increase benefits through the temporary or permanent improvement zone are subject to ensuring that the requirements of 3.06 in the restoration zone are met. Article VIII of the FMP sets out that the parties must agree to any changes arising out of FMP decisions. Should they be unable to agree the mediation process set out in the Partners' Agreement, the arbitration process outlined in the Partners' Agreement will be followed.

It is our understanding that the plan is currently in the Restoration Zone. We understand that contributions to the OTPP currently include a 1.1% special contribution on all earnings and that the Restoration Contribution Reduction under Section 3.06(e) would permit this special contribution to be eliminated.

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If the plan gets to either the temporary improvement zone or the permanent improvement zone, section 4.06 and subsection 5.05(b) of the FMP provides that a benefit improvement can only occur if the partners (the Ontario government and the OTF) have entered into a written agreement governing the manner in which the contribution by the government and other employers may be adjusted to offset any surplus distribution or benefit improvement (temporary or permanent) to be granted.

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History of Surplus

The FMP was not established until 2003. The following is a summary of the history of how surpluses were treated before the FMP and post the FMP (on a funding valuation basis).

Valuation Date	Surplus/(Deficit)	OTF	Ontario Government	Surplus Remaining
1990	$(7.8 billion) unfunded liability	Increased contributions by 1% to 8.9%	Agreed to make a series of special payments to eliminate the unfunded liability and match increased contributions	Special payments considered an asset bringing the plan to a $0 surplus
1993	$1.5 billion	$325 million to offset social contract days	Eliminated special payments for $1.2 billion saving	$0

1996	$0.7 billion	$0.6 billion for benefit improvements and RCA contributions	N/A	$0.1 billion
1998	$6.8 billion	$2.2 billion for benefit improvements	$4.6 billion to reduce the value of remaining special payments	$0
1999	$3.5 billion	N/A	$3.5 billion to reduce the value of remaining special payments	$0
2001	$6.8 billion	$6.2 billion for benefit improvements	N/A	$0.6 billion
2002	$1.9 billion	Sponsors agreed not to make any changes to benefits or contributions		$1.9 billion
Total		**$9.3 Billion**	**$9.3 Billion**	

* Source: Ontario Teachers' Pension Plan Board "Report on Funding" (April 2002)

Year	Valuation Status and Key Decisions
2003	$1.5 billion surplus; no changes to benefits or contribution levels. Funding Management Policy adopted by plan sponsors.
2005	A preliminary $6.1 billion shortfall was resolved, leaving plan with a $0.1 billion surplus. Shortfall resolved with special contribution rate increases, totalling 3.1% of base earnings by 2009 for teachers, the Ontario government and other employers. OTF used the $76 million contingency reserve set aside in 2001 to reduce contribution rate increases for members in 2008.
2008	A preliminary $12.7 billion shortfall was resolved with the introduction of conditional inflation protection for pension benefits earned after 2009 and an increase in the basic contribution rate for members and the government to 9% from 8%. Employers agree to make special payments equal to any annual pension increases retirees forgo to a maximum of 50% missed inflation.
2009	A preliminary $2.5 billion shortfall was resolved primarily by assuming a slightly higher long-term rate of return on investments: yield on real-return bonds plus 1.5%, versus real-return bonds plus 1.4%. Other minor changes made to assumptions to reflect recent plan experience.
2011	A preliminary $17.2 billion shortfall was resolved with a 1.1% contribution rate increase (phased in over three years), slightly smaller annual cost-of-living increases for teachers who retired after 2009, and recognition of current contribution rate as the permanent base rate.
2012	$9.6 billion preliminary shortfall adjusted to reflect changes in mortality assumptions and impact of two-year freeze on teachers' salaries. 2012 shortfall resolved by making inflation protection for pension credit earned after 2013 fully conditional on plan's funded status and providing slightly smaller pension increases, beginning in 2014, for members who retired after 2009. These changes enabled the plan to assume a slightly higher discount rate. The changes left the plan with a $200 million surplus at Jan. 1, 2012.

2014	$5.1 billion preliminary funding surplus used to boost pensions of members who retired after 2009 to the level they would have been at if full inflation protection had been provided each year since they retired. The surplus funds were also used to raise conditional inflation protection to 60% of the increase in the cost of living for the portion of retirees' pensions earned after 2009. Both changes are effective with January 2015 pension payments.
2015	Some of the $6.8 billion preliminary funding surplus was used to boost pensions of members who retired after 2009 to the level they would have been at if full inflation protection had been provided on January 1, 2015. The surplus funds were also used to raise conditional inflation protection for pension credit earned after 2009 to 70% from 60% of the increase in the cost of living. Both changes were effective January 2016. In addition, some surplus funds were reserved to help facilitate stability in contribution and benefit levels should a future funding valuation show a decline in assets or increase in pension costs.
2016	Some of the $13.2 billion funding surplus will be used to boost pensions of members who retired after 2009 to the level they would have been at if full inflation protection had been provided on January 1, 2016. The surplus funds will also be used to raise conditional inflation protection for pension credit earned after 2009 to 90% from 70% of the increase in the cost of living. Both changes will be effective January 2017. Some funds will also be reserved to increase the stability in contribution and benefit levels, should future valuations show a decline in asset value or an increase in pension costs.

* Source: Ontario Teachers' Pension Plan, "Key Funding Decisions Since 1990" adapted for September 14, 2016 announcement.

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Impact of Restoring Inflation Indexation

As noted above, the concept of conditional inflation protection was introduced in 2008 and relates to pension benefits earned after 2009. If inflation protection is reduced, the government would make extra payments equal to the amount of inflation protection forgone by retired teachers, up to 50% or above. These additional payments are often referred to as the "share the pain" payments. If inflation protect is restored, the government's share the pain payments would be reduced concurrently and accordingly.

Despite conditional inflation protection, the accounting valuation continues to assume that 100% inflation protection will be provided. This means that the cost of indexation is being fully reflected in the measurement of the accrued benefit obligation associated with the plan on the grounds that it is the intention of the Partners to restore indexation when funding is sufficient.

As also noted in the table above, plan surpluses arising in 2014-2016 are being used to restore some of the inflation protection that was reduced in previous years. This restoration of inflation protection is fully contemplated in the FMP under Section 3 describing the Restoration Zone. The direct impact of this action is that a portion of the "share the pain" payments that would otherwise be required have been eliminated. The estimated value of this reduction in contributions is $4.3 billion related to the 2016 action ($1.85 billion for 2015, and $1.95 billion for 2014).

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