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PENSION ASSET EXPERT ADVISORY PANEL

[DRAFT] REPORT

[NTD - o/s Cover letter? (including mandate summary)

Executive Summary]

Mandate of the Panel

The Pension Asset Expert Advisory Panel (the Panel) was formed to consider:

- The requirement regarding control with respect to recognizing a pension asset for a joint defined benefit plan
- The requirement regarding control with respect to recognizing a pension asset for other pension plans
- Appropriate valuation techniques to measure a pension asset that take into consideration future decision making authority by plan sponsors
- Recommendations to the Employee Future Benefits Task Force of the Public Sector Accounting Board regarding issues that should be considered in its review of the retirement and post-employment benefits standards.

The Panel looked at certain jointly sponsored pension plans (specifically, the Ontario Teachers' Pension Plan (OTPP) and the Ontario Public Service Employees' Union Pension Plan (OPSEUPP), individually a "Plan" and collectively the "Plans") and considered whether there is a basis for recognizing a net pension asset for either or both of the Plans in accordance with Canadian public sector accounting standards (PSAS). If so, the Panel also considered how such an asset would be measured.

The recognition and measurement of pension assets arising in other pension plans, specifically the Healthcare of Ontario Pension Plan (HOOPP) and the Colleges of Applied Arts and Technology Pension Plan (CAATPP), will be covered in a later supplemental report that considers the distinct attributes of these multi-employer plans.

All pension plans examined by the Panel are defined benefit plans.

Nature of the pension plans examined

Pension plans are not all alike. Each pension plan examined by the Panel has distinct arrangements that shape how accounting guidance is applied. A detailed understanding of plan specific governance mechanisms and funding policies is essential to assessing the appropriateness of the accounting for each plan. The present contractual agreements are used for assessing existing rights and powers under the arrangements.

Under pension legislation (the *Ontario Pension Benefits Act* (the “Ontario PBA”) in Ontario), there are several categories of defined benefit plans. Jointly sponsored pension plans are a separate category from single sponsor plans or multi-employer plans and have different regulatory requirements. Both Plans are jointly sponsored pension plans, as the Ontario Provincial Government has entered into contractual arrangements with the employee sponsor of each Plan that govern the relationship between the Plan’s joint sponsors, including with respect to plan surpluses and deficiencies. The relevant legislation and contractual arrangements governing the Plans that were considered by the Panel are listed in Appendix A and key facts have been summarized below for each Plan.

Under PSAS, there are also several categories of defined benefit plans, including “Joint Defined Benefit Plans” (JDBPs). In a JDBP the government (employer) sponsor shares risks and benefits of a defined benefit plan on an equitable basis with plan participants, represented by an employee sponsor or sponsors. A key characteristic of a JDBP is a formal agreement between the sponsors which establishes shared control over the plan. Other essential characteristics of JDBPs include:

- Funding contributions are shared mutually between the government and plan members
- The sponsors have shared control over decisions related to the level of benefits and contributions on an ongoing basis based on the terms of the contractual agreement as well as arrangements for the administration of the plan
- The sponsors share, on an equitable basis, the significant risks and benefits, both positive and negative, associated with the benefit plan. The government does not retain the residual risks of the plan.

By definition, neither sponsor has unilateral control over a JDBP; shared decision making is an essential attribute. A fundamental difference between single sponsor defined benefit plans and joint sponsor defined benefit plans is that the ability a single sponsor has over setting contribution rates and benefits has been replaced with shared control over those decisions. In other words, plan oversight rests with two sponsors that must work together instead of one sponsor. The sharing of the risks of the pension plan on an equitable basis is commensurate with the sharing of control over those policies that influence the outcomes of the pension plan and the shared funding responsibilities. [REF: PS 3250.GLOSSARY]

OTPP was a single employer sponsored plan until 1992 when it was converted to be a jointly sponsored pension plan for regulatory purposes under the Ontario PBA and a joint defined benefit plan for accounting purposes. OPSEUPP was separated out of the Public Service Pension Plan (a single sponsor plan) in 1995 and established as a jointly sponsored pension plan for regulatory purposes under the Ontario PBA and a joint defined benefit plan for accounting purposes.

The motivation for making these changes was for the Ontario Provincial Government to transfer a share of the risks and costs of the obligation to the members of the plans. In exchange for taking on a share of the risk and cost of the obligation, the members received an equitable share of any surplus in the plan (both the upside and downside of plan performance are equitably shared) and the member Sponsors received the right to participate in shared control of the plan, meaning that the arrangement contemplates ongoing discussions between the sponsoring parties and joint decision-making about issues decisions such as plan structure, benefits available under the plan, contribution rates, funding levels and other policy decisions.

As both the funding risk and rewards and the governance of the Plans are shared between the employer sponsor and the employee sponsor the move from a single sponsored plan to a jointly sponsored plan was considered by all parties to be a fair and equitable arrangement for both sides.

OTPP – Structure and organization

Sponsors

The OTPP is a jointly sponsored pension plan.

The joint sponsors are the Ontario Provincial Government (represented by the Minister of Education and Training) as the employer Sponsor and the Ontario Teachers' Federation (represented by its Executive) as the employee Sponsor. The Partners' Agreement between the joint sponsors sets out how shared control is achieved and governs all aspects of the plan.

Other employers also participate in the plan, such that the OTPP is also a multi-employer plan, but these employers are not sponsors.

Decision making

The OTPP Board is appointed by the joint sponsors and is responsible for the administration of the pension plan and investment of the pension fund. It develops and implements an investment strategy, pays pension benefits, authorizes the preparation of actuarial valuations and generally manages the pension plan and fund.

The Board does not make any fundamental decisions regarding benefits and contributions as these decisions rest with the joint sponsors' Partners Committee, to which an equal number of representatives are appointed by each sponsor.

Funding arrangements

A basic funding provision, set out in the Teachers' Pension Act, is that the employers' contributions for the current year must not exceed those made by the members in the year before the preceding year.

Historically, the Employers have matched the members' contributions, based on the members' contributions in the year before the previous year. This has resulted in contributions being made typically on a 50:50 basis between employers and members (except where specifically agreed otherwise).

A limited exception to the matching contribution provisions also reflects the sharing principle underlying the OTPP. In the event that conditional indexation benefits are not paid by the OTPP in a year, the amount of this benefit reduction is matched by a corresponding contribution from OTPP employers.

The contractual arrangements require an actuarial valuation for funding purposes to be prepared at least once every three years to comply with the Ontario PBA. This actuarial valuation must be "actuarially balanced" which means that the benefits and costs to be paid from the fund plus any contingency reserve must equal the value of the plan assets, including the present value of the members' and employers' contributions plus any special payments. Procedurally, the triennial valuation process commences with a preliminary valuation prepared by the Board's actuary based on the existing terms of the plan. To the extent that this preliminary valuation is not actuarially balanced as defined above, the joint sponsors must negotiate and agree what changes to the plan must be made in order to reach an actuarially balanced valuation that will subsequently be filed. This process means there is no funding surplus or deficit in the final funding valuation that is filed to comply with the Ontario PBA.

The joint sponsors could agree to changes to the Plan to increase or decrease contributions for employers and/or members or to improve benefits payable to members or keep a contingency reserve in the Plan. Negotiations must be carried on in good faith and if an agreement is not reached within a certain time frame a mediator may be appointed by the joint sponsors, and, if necessary a board of arbitration. However, under the Partners' Agreement, agreement must be reached on how to actuarially balance the required funding valuation. The "status quo" could not be maintained if it resulted in an imbalance between the promised benefits and any contingency reserve and the plan assets, including the value of future contributions.

The joint sponsors have agreed to a Funding Management Policy (FMP) to supplement the Partners' Agreement, which sets a framework for the sponsors in jointly determining the use of any funding surpluses or the funding of deficits. The FMP, in combination with the *Income Tax Act (Canada),* requires that once the OTPP meets certain funding thresholds, the Partners must negotiate either to lower contributions or provide temporary or permanent benefit enhancements (or some combination of the two). By mutually agreeing the funding thresholds in the FMP, the Partners have agreed in principle as to when changing benefits or contributions will be taken as opposed to using or creating contingency reserves. However the FMP does not specify whether contributions, benefits or both would be adjusted. This would be subject to the negotiations by the partners and must be on an equitable basis (consistent with the definition of a JDBP).

Neither the OTPP plan text nor the FMP limits the outcomes of the negotiation between the joint sponsors. There is no minimum level or fixed range of contributions by members or employers that cannot be changed through the negotiations.

OPSEUPP – Structure and organization

Sponsors

The OPSEUPP is a jointly sponsored pension plan.

The joint sponsors are the Ontario Provincial Government (represented by the Chair of the Management Board of Cabinet) as the employer Sponsor and the Ontario Public Service Employees' Union as the employee Sponsor. The joint sponsors established a trust (OPTrust) and the declaration of trust between the joint sponsors and the trustees of OPTrust sets out how shared control is achieved and governs all aspects of the plan.

Decision making

The Board of Trustees administers the plan and an equal number of trustees are appointed by each of the Ontario Provincial Government and OPSEU.

The Board of Trustees makes decisions by majority vote. This means that at least one Trustees representing each of the Ontario Provincial Government and OPSEU must agree to a resolution in order for it to be adopted. In the case of a deadlock there are agreed upon procedures to appoint a temporary 11th trustee, as agreed by both the sponsors (or, if necessary, appointed by the Chief Justice of Ontario).

The Board of Trustees is responsible for the administration of the OPSEUPP and the investment of the OPSEU Pension Fund. It develops and implements an investment strategy, pays pension benefits, authorizes the preparation of actuarial valuations and generally manages the pension plan and fund.

The Board of Trustees has no power to amend the plan or the trust agreement. All decisions regarding contribution levels and benefits to be provided under the plan, including those made to comply with the Ontario PBA minimum funding rules are the responsibility of the sponsors.

Amendments to the trust agreement, plan text and sponsorship agreement require unanimous written consent of the sponsors.

Funding arrangements

The basic contribution requirement under the OPSEUPP text is that employers match the contributions of the members, subject to a two month lag. [s.4.6 of OPTrust Plan Text]

The Board of Trustees, and the Plan actuary, are responsible for the Plan's actuarial valuations and the actuarial assumptions used in those valuations. While valuations must be filed with the pension regulator every three years under the Ontario PBA, the Board of Trustees may elect to file a valuation more frequently [s1.3 of OPTrust Funding Policy].

In the event that a funding valuation discloses net actuarial gains after non-defrayed obligations have been met, those net actuarial gains are equally divided between an Employer 'Rate Stabilization Fund' (RSF) and a Member RSF [s.56(c) and s.57 of OPTrust Sponsorship Agreement]. Through collective bargaining, an allocation of funding surpluses on a basis that is different from 50/50 may be agreed. The Panel understand that currently no different basis of allocating funding surpluses has been agreed. The Ontario Provincial Government may retain its RSF as a reserve or use the Employer RSF to reduce its special payments or its normal costs and OPSEU may retain its RSF as a reserve or utilize its RSF in its discretion, subject only to the provisions of the Ontario PBA and the *Income Tax Act (Canada).* The OPTrust Board of Trustees has no authority with respect to the use or application of either RSF, but has recommended to OPTrust's sponsors that each RSF not exceed 12.5% of net actuarial liabilities [5.2 of OPTrust Funding Policy]. There are no restrictions on how each party bargains the use of their surplus. There is no minimum level or fixed range of contributions by members or employers that cannot be changed by agreement of the joint sponsors or through the use of their respective surplus portions.

In the event of a funding deficiency, member and employer contributions are increased equally to fund the deficiency [s.58 of OPTrust Sponsorship Agreement]. The only exception is in the event that either of the joint sponsors has an RSF and chooses to apply it to offset its share of a funding deficiency. In principle, with a sufficient RSF, either OPSEU or the Ontario Provincial Government could reduce their contributions to zero, without requiring any consent from the joint sponsor.

The plan text [s.6.4] clearly states that no amount of surplus shall be paid out of the plan to the Ontario Provincial Government or any participating employer. Contribution holidays, however, are not treated as a surplus withdrawal, and are clearly permissible under the OPTrust Sponsorship Agreement and Plan Text.

Panel view

Both OTPP and OPSEUPP have been accounted for as joint defined benefit plans in the Public Accounts of Ontario accordance with PS 3250, *Retirement benefits* since that standard was issued in 2001. The Auditor General (AG) also agrees with this classification of both plans.

The Panel agrees with the accounting classification of both plans as joint defined benefit plans.

Determination of relevant accounting guidance and assessing accounting policies applied to pension plans

The accounting analysis is performed in accordance with Public Sector Accounting Standards (PSAS) issued by the Canadian Public Sector Accounting Board (PSAB). PSAB was created to establish accounting standards specifically tailored for the public sector.

PSAS identifies sources of guidance to be used in determining appropriate accounting policies in PS 1150, *Generally Accepted Accounting Principles*. First, a government must follow any specific standard that relates to the issue under consideration, that is, to apply every primary source of Generally Accepted Accounting Principles (GAAP). In this case, PS 3250, *Retirement benefits* (PS 3250) is a standard that specifically addresses the accounting for defined benefit pension plans. Further, PS 3250 also defines and contains specific guidance on accounting for joint defined benefit plans.

If the concepts of PS 1000 *Financial Statement Concepts* (PS 1000) are found to conflict with a primary source of GAAP, the primary source of GAAP prevails [PS 1150.12]. If a primary source of GAAP may be interpreted in more than one way, the government selects the treatment that is most consistent with the principles of the primary source of GAAP [PS 1150.14].

If a primary source of GAAP, such as PS 3250, is not clear, the government develops an accounting policy considering other standards within PSAS and PS 1000. Recently PSAB has undertaken a project to review and update its conceptual framework in PS 1000. While this project is on-going, PSAB has issued a number of standards to expand on and clarify the guidance provided in PS 1000 on Assets, Contingent Assets and Contractual Rights. These standards are not mandatorily effective until April 2017, but early adoption is permitted and as such, they are valid sources of reference as they were developed to be consistent with PS 1000.

A government may also refer to accounting guidance in other GAAP frameworks as long as those frameworks are consistent with PSAS standards and PS 1000 above. PS 1150 identifies the Canadian Accounting Standards Board (AcSB), International Accounting Standards Board (IASB), and International Public Sector Accounting Standards Board (IPSASB) amongst others, as important sources to consult on matters not covered by primary sources of GAAP or for assistance in applying a primary source of GAAP to specific circumstances. [PS 1150.19]. In addition, PS 1000 states that the objectives of government financial statements are a significant factor in the selection of accounting policies used in government financial reporting [PS 1000.13]. The objectives of government financial statements are set out in PS 1100, *Financial Statement Objectives* and are consistent with PS 1000 concepts. They are therefore a relevant source of guidance when determining appropriate accounting policies.

In considering the recognition and measurement issues addressed in this report, the Panel considered both the concepts in PS 1000 and the objectives of financial statements in PS 1150, as well as relevant guidance issued by other standard setters, and particularly were guided by the following principles and objectives:

➢ Financial statements are prepared to provide useful information

Financial reporting is not an end in itself. Its purpose is to communicate useful information to users of general purpose financial statements (GPFSs). Governments are accountable to those that provide them with resources, and to those that depend on them to use those resources to deliver services during the reporting period and over the longer term.

The objectives of financial reporting by governments are, therefore, to provide information about the government that is useful for accountability purposes and for decision-making purposes. Among other things, users of the GPFSs of governments need information to support assessments of the resources currently available to support present activities, meet liabilities and contractual obligations and for future expenditures to support service delivery activities, and to what extent there are restrictions or conditions attached to their use.

➢ What qualities make financial statement information useful?

The most important qualities that make information useful to users are relevance and faithful representation. For it to be useful, the information must be relevant to the decisions made by users and for assessing accountability. That is, it has the potential to make a difference to those decisions and assessments.

Accounting uses the term “faithful representation” to mean that the information provides an authentic or realistic portrayal of the economic phenomena it says it portrays. For this to be the case, the transactions and other events reflected in the financial statements must be accounted for, presented and described in accordance with their substance and economic reality at the time they are included in those statements.

Thus, when a potential accounting treatment is being evaluated, it is assessed in large part by considering whether it will produce information that is relevant and that provides a realistic picture of the government. This requires financial statements that show clearly the government’s assets and liabilities, income and expenses.

An important component of faithful representation is neutrality. Information is neutral when it is free from bias that would lead users towards making decisions that are influenced by the way the information is measured or presented. Financial statements that do not include everything necessary for faithful representation of transactions and events affecting the entity would be incomplete and, therefore, potentially biased.

Neutral information faithfully represents the economic and other phenomena that it purports to represent. However, to require information included in GPFSs to be neutral does not mean that it is without purpose or that it will not influence behavior. Relevance is a qualitative characteristic and, by definition, relevant information is capable of influencing users’ assessments and decisions.

➢ What place “conservatism”?

PS 1000 describes conservatism this way:

> Conservatism
> The application of conservatism in making judgments under conditions of uncertainty affects the neutrality of financial statements in an acceptable manner. When uncertainty exists, estimates of a conservative nature attempt to ensure that assets, revenues and gains are not overstated and, conversely, that liabilities, expenses and losses are not understated. Conservatism does not, however, encompass the deliberate understatement of assets and revenues or the deliberate overstatement of liabilities and expenses.

A similar discussion of the same concept, labelled “prudence”, was included in the pre-2010 conceptual framework of the IASB. In finalizing the new version of its Framework in 2010, the confusion caused by the ambiguity of that discussion prompted the IASB to remove any reference to prudence and to describe in other ways the desirable characteristics of good quality financial reporting. However, after much comment and debate, in its most recent Exposure Draft (ED) of changes to its conceptual framework, the IASB proposed re-introducing an explicit reference to “prudence”. The Basis for Conclusions to that ED provides the following rationale for that proposal:

> The IASB noted that prudence is a term used by different people to mean different things. In particular:
>
> (a) some use it to refer to a need to be cautious when making judgements under conditions of uncertainty, but without needing to be more cautious in judgements relating to gains and assets than for those relating to losses and liabilities ('cautious prudence').
>
> (b) others use it to refer to a need for asymmetry: losses are recognised at an earlier stage than gains are ('asymmetric prudence'). There is a range of views on how to achieve such asymmetry, and to what extent. For example, some advocate a concept of prudence that would:
>
> > (i) require more persuasive evidence to support the recognition of gains (or assets) than of losses (or liabilities); or
> >
> > (ii) require the selection of measurement bases that include losses at an earlier stage than gains.
>
> The IASB considers that prudence (defined as the exercise of caution when making judgements under conditions of uncertainty) can help achieve neutrality in applying accounting policies. Thus, cautious prudence is a factor in giving a faithful representation of assets, liabilities, equity, income and expenses.
>
> Some argue that asymmetric prudence is a necessary characteristic of useful financial information. The IASB disagrees with this view.

In the ED and its subsequent consideration of comments received, the IASB has concluded that only "cautious prudence" is consistent with neutrality, and therefore with faithful representation of financial information. PSAB's 2015 consultation paper on *Conceptual Framework Fundamentals and the Reporting Model* is consistent with the conclusions of the IASB:

> Conservatism is removed as an explicit concept but would still play a role in cases of estimation when there is uncertainty and there is a choice between equally possible amounts. In such cases, conservatism would require that there be no deliberate understatement of liabilities or overstatement of assets.

This view of applying a "cautious" conservatism in respect of estimation uncertainty rather than as a rationale for asymmetrical recognition or measurement of assets or liabilities is consistent with the current definition of conservatism in PS 1000, and represents the latest thinking of standard setters in a number of jurisdictions, including Canada.

➢ What is the definition of an asset under PSAS

Faithful representation and the need for useful information entails that only items that meet the definition of an asset under PSAS should be recognized in the financial statements.

As defined in PS 1000 and PS 3210, *Assets*, assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained. Assets may be financial resources or non-financial resources. Assets have three essential characteristics:

(a) they embody future economic benefits that involve a capacity, singly or in combination with other assets, to provide goods and services, to provide future cash inflows, or to reduce cash outflows;

(b) the public sector entity can control the economic resource and access to the future economic benefits; and

(c) the transaction or event giving rise to the public sector entity's control has already occurred. [PS 1000.35-.36]

For an asset to exist a government must control the future economic benefit associated with the asset to the extent that it can benefit from the asset and generally can deny or regulate access to that benefit by others. This guidance was expanded by PS 3210, a standard that is effective from April 1, 2017, which clarifies that a government controls an economic resource and access to its future benefits when it can benefit from the economic resource through its capacity to provide goods and services, to provide future cash inflows or to reduce cash outflows, deny or regulate access to those benefits by others, and is exposed to the risks associated with the economic resource. [PS 3210.16, related archived pronouncement PS 1000.38]

IPSAS 39, *Employee Benefits* explains how the basic definition of an asset is met for a net pension asset. Although it does not apply this definition to a JDBP, it provides a helpful perspective on how to assess the conceptual definition of an asset, including control, economic benefit and risk concepts to that of a pension asset which typically exists in a separate vehicle, a trust, from the sponsors. IPSAS 39.67 notes that an asset exists when a plan has been overfunded or where actuarial gains have arisen (i.e. when there is a surplus for accounting purposes), and that an asset arises because the entity controls a resource - the resource being the surplus that generates future benefits and the control being the ability to use the resource. In addition, future economic benefits are available to the entity in the form of a reduction in future contributions or a cash refund, either directly to the entity or indirectly to another plan in deficit. The asset ceiling is the present value of those future benefits. Control is as a result of past events (contributions paid by the entity and service rendered by the employee). [Taken from IPSAS 39.67 – actual wording in appendix B]

The economic resource in question is the accrued benefit asset that arises from applying the accounting guidance in measuring plan assets and the accrued benefit obligation, including the provisions regarding the deferral of unamortized gains or losses. The accrued benefit asset may be very different from any surplus calculated under an actuarial valuation performed for funding purposes. Funding valuations use different actuarial methods and assumptions, such as a provision for adverse deviations. However, under accounting standards any surplus represents the best estimate of the accrued benefit obligation and the fair value of the plan assets, as adjusted for the permitted deferral provisions. PS 3250 – the primary source of GAAP for retirement benefit plans – clearly requires an accrued benefit asset to be recognized for a defined benefit pension plan regardless of whether there is a surplus calculated for a funding valuation and notwithstanding the delayed recognition of actuarial gains and losses due to the deferral provisions and the measurement uncertainty regarding both the measurement of the plan assets and the accrued benefit obligation.

PS 1000 also provides the following recognition criteria:

a) That the item has an appropriate basis of measurement and a reasonable estimate can be made of the amount involved; and

b) For an items that involved obtaining or giving up future economic benefits, it is expected that such benefits will be obtained or given up. [PS 1000.55]

This second criteria requires that future economic benefits are *expected* but do not need to be certain. PS 1000 states that:

> "Expected" is used with its usual general meaning an refers to that which can be reasonably be anticipated, contemplated or believed on the basis of available evidence or logic but is neither certain nor proved. The use of the word in the recognition criteria is intended to acknowledge that economic activities occur in an environment characterized by uncertainty" [PS 1000.56]

An item must first meet the definition of an asset (or other element) under PS 1000, then in addition both recognition criteria must be met.

PS 3250 provides an appropriate basis of measurement for a net pension asset. Additionally, PS 3250 also requires a net pension asset to meet the general recognition criteria, by defining what are *expected future benefits* in the context of defined benefit pension plans [PS 3250.GLOSSARY].

Panel View

The Panel considered the guidance in PS 3250 and how it applies to the recognition and measurement of government's share of the Plans when they are in an accrued benefit asset position for accounting purposes. In its analysis the Panel considered whether the contractual arrangements and other circumstances regarding the government's share of an accounting surplus in the Plans met the definition of an asset and whether the resulting accounting meets the financial statement objectives of PSAS.

The Panel's analysis is presented in the following sections on Recognition Issues and Measurement Issues.

Recognition issues

1) Application of Defined Benefit accounting to Joint Defined Benefit Plans

PS 3250 Paragraph 81 states "When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans".

The Panel discussed two possible interpretations of how this guidance is to be applied to JDBPs:

- Interpretation A) Divide the plan between the sponsors' respective portions; the government applies the guidance on defined benefit plans in PS 3250 only to its portion;
- Interpretation B) The government applies the defined benefit plan guidance in PS 3250 to the plan as a whole; then recognizes only its portion of the plan in its financial statements

This is a critical interpretation in assessing both the asset recognition guidance in PSAS and the perspective through which the guidance on defined benefit plans in PS 3250 is applied.

For example, under interpretation A, dividing the plan first would entail measuring plan assets at the government's share, determining the accrued benefit obligation at the government's share and then applying the valuation allowance to any net accrued benefit asset that arises. Both the Ontario Provincial Government and AG seem to implicitly adopt this view in their analysis.

Conversely, under interpretation B, the plan assets and accrued benefit obligation amounts for the whole plan are measured in accordance with PS 3250. The valuation allowance guidance is applied to any accrued benefit asset that arises on the plan as a whole. The government then calculates its portion of the accrued benefit asset, net of any valuation allowance in determining the amount of asset to recognize in the Public Accounts.

In its analysis the Panel noted that the contractual arrangements between the Sponsors affect the plan as a whole because there is joint control over the plan as a whole and not unilateral control by each sponsor over its portion of the plan. As noted in section [x] above this is an inherent characteristic of a JDBP. For example, there is one funding policy, one Partners' agreement (OTPP) or sponsorship agreement (OPSEUPP), one plan text and so on, that govern the respective plans. Members' service and earnings are also measured as a whole, and not split between different sponsors. A determination of the assets and the obligations of a defined benefit plan can only be made with reference to the plan as a whole. To apply the guidance on the Limit on the Carrying amount of an Accrued Benefit Asset (the “Limit guidance”) to the government’s share of the plan, while applying the guidance on determining the accrued benefit obligation and the measurement of plan assets to the plan as a whole would not be a consistent approach. The Panel believes that if the PSAB had intended joint defined benefit plans to apply the valuation allowance guidance for defined benefit plan accounting to the government’s portion of the plan only they would have specified this and provided additional guidance as to how this should be applied in this context.

An important characteristic of JDBPs is that there is an equitable sharing of the plan which applies to both risks and rewards and is the underlying economic rationale for a JDBP. One of the implications of Interpretation A is that the sponsors might recognize a liability for their portion of a net liability but be unable to recognize an asset for their portion of a net asset. It would not be an equitable sharing for a sponsor to have only an obligation for a net liability without any access to a net asset position. In fact such a plan might not meet the definition of a JDBP as such a position would indicate that either residual risk rests only with one sponsor and not the other, or that neither sponsor can access the economic resources held within the plan, which would not faithfully represent the underlying risks and rewards of the arrangement which are intended to be shared on an equitable basis. The fundamental difference between a single sponsor plan and a joint defined benefit plan is that for the latter, control is shared and a sponsor has only a portion of the positive or negative risks. It would be logical and consistent with the objectives of financial reporting to calculate the plan net asset or net liability in the same manner as for single sponsor plan – on a whole plan basis – before accounting for the shared control distinction by determining what is the government’s portion that net asset or net liability.

The Panel also noted that generally defined benefit plan accounting in financial statements is based on a *net* amount of plan assets less accrued benefit obligations. Rather than presenting plan assets as “Assets” of the sponsor and plan liabilities as “Liabilities” of the sponsor, these are presented as a net asset or liability, which reflects that the plan is a separate entity. This accounting is more similar to an “equity method” of accounting which reflects the sponsor’s interest in the net assets (or net liability) of a plan than to a proportionate consolidation accounting. Therefore, it is therefore also conceptually consistent to calculate the net assets (or liabilities) in the plan in accordance with accounting standards before determining a sponsor’s portion of the plan.

Application to OTPP and OPSEPP

In respect of OTPP, the Partner's Agreement and the Plan Text set out the entitlement to gains or surplus under the plan (benefits) and the liability for deficiencies in the pension fund (risks) are shared between employers and active members, consistent with the *Teachers' Pension Act* [TPA 10 (1)]. This has historically been 50:50 when considered over the long term.

The OPSEUPP plan indicates that any actuarial gains are allocated between the employers and members on a 50:50 basis. Each sponsor can then utilize its portion as it unilaterally determines. This means that members and employers could utilize their gains at different times, as historically has been the case resulting in the portion of the plan net asset that relates to the government's share fluctuating as a percentage of the total net asset balance. As a result the Ontario Provincial Government may not have an exact 50% portion of the net pension asset at any one time, when determining what their share of the OPSEUPP asset is.

Panel View

The Panel believes it is appropriate to apply all aspects of the guidance for accounting for defined benefit plans in PS 3250 to a JDBP prior to determining the government's portion of that plan for recognition in the financial statements. This results in financial reporting for a JDBP that aligns most closely with the concepts of defined benefit accounting in PS 3250 and with the economic substance of joint defined benefit plan arrangements.

The Panel noted that the existence of different interpretations of PS 3250.81 suggests that PS 3250 is not as clear as it could be regarding the application of the defined benefit plan guidance to JDBPs. Section [x] of the report includes a recommendation to the PSAB Employment Benefits Task Force on this observation.

The Panel recommends that the Ontario Provincial Government monitor the use of its rate stabilization reserve to determine what its share of the net pension asset of OPSUEPP is, as this could fluctuate over time.

2) Definition of an asset – Is there an economic resource that the Ontario Provincial Government can benefit from?

As noted in Section [X], an accrued benefit asset (i.e. an accounting surplus in a pension plan) is an economic resource of the pension plan. For the Plans, the question is whether the accrued benefit asset is an economic resource to the Ontario Provincial Government. In other words, does the Ontario Provincial Government have the ability to benefit from the economic resource? The question of control of that ability is discussed in Section [x] below.

Consistent with the discussion in Section [x – application to JDBPs] above, a joint sponsor accounts for its portion of an accrued benefit asset in its financial statements. If application of PS 3250 to the plan as a whole results in an economic resource existing on an accounting basis (i.e., there is an accrued benefit asset, net of any valuation allowance – see Section [x – measurement]), then a joint sponsor should recognize its share of that resource under JDBP accounting. The plan arrangement would indicate what portion is the government's share and what is the employee sponsor share, but the economic resource must be equitably portioned between the two sponsors, as equitable sharing of risks and rewards is basic tenet of JDBP accounting.

Notwithstanding that the above position is the result of applying PS 3250.81 to an accrued benefit asset recognized in accordance with PS 3250.017 and PS 3250.GLOSSARY, which are primary sources of GAAP, the Panel considered whether the plan arrangements result in the Ontario Provincial Government, as a joint sponsor, having an ability to benefit from its share of the economic resource in each of the Plans and thus meeting this part of the definition of an asset.

Consistent with PS 3250.052, there are two ways that a sponsor can benefit from a pension surplus – withdrawal of the surplus which involves taking cash out of the plan (cash inflow for the sponsor), or contribution holidays, which involves reducing future contributions that would otherwise be payable for future service (reduction of cash outflows for the sponsor). In both cases the cash received from withdrawal or saved by reducing contributions is unrestricted and can be used to settle other obligations of the Ontario Provincial Government or to fund the provision of goods and services, thereby meeting the definition of future economic benefits.

There is considerable case law in Canada addressing single sponsor plans and the ability of that sponsor to either withdraw surplus from the plan or take contribution holidays. Critical to assessing the ability of the sponsor to withdraw surplus or take contribution holidays are the plan trust agreement and plan text; clear rights within the plan documents can support the sponsor's right to withdraw surplus or take contribution holidays. However, the law treats surplus withdrawals on a very different basis from contribution holidays.

Surplus withdrawals are highly regulated by the Ontario PBA, and are regulated differently depending upon whether a surplus withdrawal is being considered from a continuing plan or on plan wind-up. A threshold question in any case of withdrawal is legal entitlement or 'ownership' of surplus, and it is often the case that entitlement is not clear, and that neither the employer nor the plan members have an incontrovertible claim to a plan surplus. In Ontario, all surplus withdrawals are subject to the review and consent of the Superintendent of Financial Services. In addition, either legal entitlement to the surplus must be established or there must be an agreement between the employer, active members and retired members about the surplus withdrawal. Arbitration procedures may also be utilized in some jurisdictions to determine an allocation of surplus. Under applicable case law and the Ontario PBA, it is generally considered that a sponsor does not have a legal right to withdraw a surplus until these hurdles have been passed. Since OPSEU specifically prohibits surplus withdrawal by either of the joint sponsors, and OTPP is silent on the issue of surplus withdrawal, the joint sponsors cannot avail themselves of any surplus through withdrawal (jointly or separately).

Based on the above considerations the Panel determined that the Ontario Provincial Government, as joint sponsor, does not have any ability to access the net pension asset through surplus withdrawals.

Conversely, the Ontario PBA expressly permits contribution holidays without any requirement for Superintendent review or approval. Although certain plan provisions have been found to prohibit contribution holidays, this is the exception rather than the rule and contribution holidays are commonly taken by Canadian defined benefit plans. In general, a plan text need not expressly permit a contribution holiday in order for a plan sponsor to reduce its contribution on account of a funding surplus. It is generally the case that the plan actuary may take surplus into account in determining the required level of employer contributions; the plan actuary is only prohibited from doing so where express plan provisions require employer contributions regardless of any plan surplus.

The accounting asset arises in part because OTPP and OPSEUPP are conservatively funded in order to protect the Plan's funded status in cases of poor performance and to maintain contribution and benefit stability regardless of economic conditions. As noted in Section [x – accounting guidance] accounting valuations are "best estimate valuations" and not designed to be overly conservative as this would not result in a faithful representation of the asset or liability of the Plans. As a joint sponsor, it is reasonable for the Ontario Provincial Government (and Ontario taxpayers) to expect that fewer contributions will be needed to be made into these plans to the extent there are more assets that are required to pay the anticipated benefit obligations. Teachers/OPSEU members would also have a similar expectation on their side that they can access their portion of any surplus assets. In fact it would be unreasonable to assume that neither joint sponsor has the ability to access the surplus, given they are joint sponsors of the plan. It would be similarly unreasonable to assume that one sponsor can access the surplus to a greater extent than the other sponsor, as this would be against the principles of a JDBP and the equitable sharing objectives that are consistent with the OTPP and OPSEU plan arrangements. Rather, the economic reality of a JDBP that an economic resource exists and is shared by both sponsors for the benefit of both sponsors.

An analysis of the plan documents for OTPP and OPSEU indicate that in both plans the sponsors fund the plans on an equitable basis and therefore both joint sponsors can benefit from a reduction in contribution rates. The benefit of the plan asset can only accrue to the joint sponsors and no other third party, and the definition of a JDBP means that these benefits must be shared on an equitable basis - they will not accrue only to one of the joint sponsors. As such, it is clear that the Ontario Provincial Government has an ability to access the future benefits through contribution reductions. The question of whether the Ontario Provincial Government controls its ability to access these future benefits is discussed in Section [X – recognition 3] below.

The Panel considered whether PS 3320, *Contingent Assets* would apply. Contingent assets are defined as “possible assets arising from existing conditions or situations involving uncertainty. That uncertainty will ultimately be resolved when one or more future events not wholly within the public sector entity's control occurs or fails to occur. Resolution of the uncertainty will confirm the existence or non-existence of an asset”. A contingent asset is not recognized in financial statements because there is uncertainty as to whether an asset exists.

An accrued benefit asset is not an uncertain economic resource. While there is uncertainty regarding the measurement of an accrued benefit asset due to the necessity of making actuarial assumptions regarding demographic and financial factors as well as fair values of plan assets, there is no uncertainty as to whether the plan exists, and therefore over the underlying existence of any estimated accrued benefit asset as an economic resource. PS 3320 notes that “The mere fact that an estimate of an amount is involved (measurement uncertainty) does not, in and of itself, constitute the type of uncertainty that characterizes a contingent asset”. The extent of the economic resource becomes clear as measurement uncertainty is resolved, not as future events occur or fail to occur. For clarity, while actuarial assumptions may be revised as more information arises in respect of the cost of the services provided by employees, this is a resolution of the measurement uncertainty inherent in the estimation of services provided. There are no future events needed to clarify whether the service was provided by the employees or not or whether the plan assets were contributed or not.

As such, PS 3320 is not a relevant source of guidance in considering whether the Ontario Provincial Government can recognize an asset in respect of an accrued benefit asset in a JDBP plan.

Panel view

The accounting asset meets the definition of an economic resource because the accrued benefit asset exists and future benefit is available to the sponsors in accordance with the plan documents. There is no existence uncertainty regarding the net pension asset.

3) Definition of an asset - Control

As noted in Section [x – determination of appropriate accounting principles], an economic resource must be controlled by a government to meet the definition of an asset. The Ontario Provincial Government exercises shared control as joint sponsor for OTPP and OPSEUPP which can still meet this definition because the Ontario Provincial Government is exposed to the risk of plan surplus changing from a variation in actuarial assumptions or emerging plan experience, can benefit from the economic resource (as discussed in Section [x above] and can deny the other sponsor access to the resource to the extent that joint decisions must be made regarding the administration of the plan. The contractual arrangements for OTPP and OPSEUPP set out how that shared control is exercised, including how surpluses and deficits are dealt with and any changes to the contractual arrangements must be agreed by both joint sponsors. The effect of this is that each sponsor individually has a veto right for fundamental changes to the Plan or shared decisions that are made under the existing Plan arrangements. This shared control relationship contrasts with participating employers that are not part of the control group, as those employers are not able to regulate or deny access to the plan assets and therefore cannot control access to the economic resource of a net plan asset.

By definition, a joint sponsor of a JDBP cannot have unilateral control or unilateral rights to the surplus of a JDBP. Instead there is an agreed upon, pre-determined process. That process provides certainty that a conclusion on the use of any surplus will be reached with the expectation that the outcome of the process will be an equitable sharing of any surplus, as equitable sharing is a key characteristic of a JDBP. Shared control means that control over the plan as a whole is exercised through the joint sponsors as a control group. The contractual arrangements for OTPP and OPSEUPP set out how that joint control is exercised, including how surpluses and deficits are dealt with and, consistent with the principles of JDBPs, require an equitable sharing. Importantly, the fundamental contractual arrangements of OTPP (Partners' Agreement) and OPSEUPP (Sponsorship Agreement) cannot be changed without the consent of each of the joint sponsors. Each joint sponsor has the ability to protect its own equitable share of the Plan and thus the Ontario Provincial Government can effectively deny access to the other sponsor to the government's share, and vice versa.

As noted in Section [x – recognition 2] above, the joint sponsors do not (either separately or collectively) have an existing legally enforceable right to benefit from a plan asset through a withdrawal of surplus. Rather, the ability of the joint sponsors to benefit from the plan is through contribution holidays. Under the terms of each Plan, the joint plan sponsors have the joint right to contribution reductions and holidays as a means to use any surplus assets in the plans. This means that collectively the sponsors can exercise their shared control to reduce future contributions to the plan and access their portion of the economic resource in the form of future economic benefits. No other parties need agree to these contribution reductions and the control elements of the asset definition is met on a joint basis.

Other sources of GAAP within PSAS also support that shared control is sufficient for asset recognition. PS 3060 requires asset recognition for government business partnerships subject to shared control using the modified equity method. PS 3060 requires proportionate consolidation for other government partnerships – a model which results in a government recognizing a proportionate share of the capital assets held under joint control, for example, even though the government cannot control the use of that asset unilaterally. If a jointly controlled asset cannot meet the recognition criteria for an asset then it would logically follow that no investments in government partnerships could be recognized. As it is, such assets are recognized by governments applying PSAS in their public accounts. In other words, it is a clearly acceptable concept under PSAS that shared control is sufficient to justify the recognition of a portion of an asset that is under shared control. It seems logical that this concept should also apply to a pension asset of a JDBP. In the context of PS 3250, and consistent with the Panel's views expressed in Section [X – recognition 1] the defined benefit guidance is to be applied to each plan, and then the members of control group each pick up their share.

Panel view

Unilateral control in a JDBP is not a requirement for asset recognition. An asset subject to joint control can be recognized under PSAS. The joint sponsors jointly control the entire net pension asset, and can recognize their portion of that jointly controlled asset.

4) Recognition criteria – Expectation that future economic benefits will be obtained

In addition to the analysis performed under PS 3250, the Panel considered if the recognition criteria of PS 1000 were met for the Ontario Provincial Government's share of the net pension asset.

For OTPP, the plan terms may be negotiated to increase (or decrease) contributions or increase (or decrease) plan benefits. The past history of the sharing of plan surpluses between the Ontario Provincial Government and the Ontario Teachers' Federation (OTF) indicates that on the side of the Ontario Provincial Government the equitable sharing of surpluses as resulted in reductions of Employer contributions, even while the

OTF has negotiated increases in member benefits in respect of utilizing their equitable share of any surplus. [REF: Appendix G of the Ontario Provincial Government's position paper]. While there is no certainty as to the form of future benefit that future negotiations will take, this history indicates that the Ontario Provincial Government has been able to negotiate reductions in contributions in the past and supports an expectation that they would be able to do so in the future, given their negotiating rights under the Partners' Agreement and the requirement that the risks and benefits of the plan be shared equitably.

For OPSEUPP, the "rate stabilization reserves" mechanism also supports that the Ontario Provincial Government has a valid expectation of being able to benefit from any plan surplus that arises as the reserves can be used to reduce future contributions.

The application of the specific definition of "expected future benefits" in PS 3250 is discussed further in Section [x – measurement] below. If the application of PS 3250 results in "expected future benefits" sufficient to supports a net pension asset, then by definition, this asset would meet the recognition criteria in PS 1000.

Both the OTPP and OPSEUPP have unamortized (unrecognized) actuarial gains as at March 31, 2016 which, when recognized, will increase the accounting amount of the accrued benefit asset. To the extent that there are expected future benefits in excess of the accrued benefit asset these would not be recognized under PS 3250, even though a reasonable estimate of the amount of the expected future benefits could be made. Conversely, the Panel observes that when a plan has unamortized actuarial losses an accrued benefit asset may be recognized in excess of any amount of expected future benefit as calculated by PS 3250, as the specific recognition provisions in PS 3250 override the conceptual requirements for expected future benefits in respect of unamortized actuarial losses that have not yet been recognized. The Panel notes that the current PS 3250 requirements are applied to pension plans, as PS 3250 is a primary source of GAAP. However, the Panel recommends that the inconsistency between the recognition criteria in PS 1000 and the requirements of PS 3250 is addressed by the PSAS Employment Benefits Task Force. Section [x] of the report includes a recommendation to the PSAB Employment Benefits Task Force on this observation.

Panel view

For both OTPP and OPSEUPP the general recognition requirement of "expected future benefit" is met.

Panel View – Recognition issues

PS 3250 requires the recognition of an asset for the government's portion of the plan surplus for both plans. This is consistent with the financial statement concepts of PSAS including the definition of an asset and the recognition criteria in PS 1000. For the Ontario Provincial Government to recognize a liability for portion of a net liability but be unable to recognize an asset for their portion of a net asset which represents a true economic resource, would not faithfully represent the economics of a JDBP whereby the risks and rewards of the plan are shared between the Joint Sponsors.

Those assets may require a valuation allowance. The measurement of those assets is addressed in the next section.

Measurement issues

Overview of guidance on measurement of an accrued benefit asset

PS 3250 paragraphs 50 to 59 provide guidance on measuring any accrued benefit asset that results when the plan assets are measured at an amount greater than the accrued benefit obligation. This is known as the "Limit on the carrying amount of an accrued benefit asset" (the "Limit guidance" or "Valuation allowance"). Consistent with the Panel's views in Section [x – recognition 1] the guidance on defined benefit plans is applied to JDBPs prior to the government recognizing its portion of the plan. The Limit guidance should also be applied to the plan as a whole, prior to the joint sponsors recognizing their respective portions of the result.

PS 3250 defines an accrued benefit asset as "the amount of any asset recognized on a government's statement of financial position in respect of employee retirement benefits before deducting any valuation allowance that may be required. It is the sum of the government's accumulated cash contributions less the sum of the current and prior years' benefit expenses (before any change in the valuation allowance)." [PS 3250.GLOSSARY]

Any accrued benefit asset is adjusted for net unamortized losses, before testing for the valuation allowance, to give an adjusted benefit asset. "Adjusted benefit asset is an accrued benefit asset less the amount, if any, by which the aggregate of any unamortized actuarial losses exceeds the aggregate of any unamortized actuarial gains." This is because the net unamortized losses will reduce the accrued benefit asset over time as these losses are recognized. No adjustment is made for net unamortized gains as these would increase the accrued benefit asset, which would be inconsistent with the accounting model in PS 3250. In the case of OTPP and OPSEUPP there are net unamortized gains, and so the accrued benefit asset equals the adjusted benefit asset.

PS 3250 requires the *expected future benefit* to be compared to the adjusted benefit asset [3250.54], and specifies how the expected future benefit is to be calculated:

A government determines its expected future benefit as the sum of:

a) the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus; and
b) the amount of the plan surplus that can be withdrawn in accordance with the existing plan and any applicable laws and regulations. [PS 3250.56]

The difference, if any, by which, the adjusted benefit asset exceeds the expected future benefit is the amount of the valuation allowance, which is recorded against the accrued benefit asset with a corresponding amount recognized in the statement of operations.

1) Impact of legally enforceable rights on calculation of expected future benefit amount

As noted in Section [x – recognition – 4] above, the objective of the Limit guidance in PS 3250 is to ensure that any asset recognized is measured at an amount that can be realized in the future, or in other words, the expected future benefits that can be obtained from the asset. [PS 3250.55] Under the standard there are two ways that expected future benefits may be realized – through the withdrawal of surplus or through using the surplus to pay for benefits earned by members in future periods – that is, paying lower contributions into the plan in the future, often referred to as a “contribution holiday”.

The Panel did not put any emphasis on expected future benefits arising from withdrawal of plan assets, as the Ontario Provincial Government does not expect to benefit from surpluses through a withdrawal, and there is no explicit right for the sponsors to claim a withdrawal from the plans. This is consistent with the discussion in Section [x – recognition 2] above. PS 3250 paragraph 59 requires a legally enforceable right to exist before an expected future benefit can be recognized for a withdrawal or surplus. The Panel believes that these requirements apply specifically to the expected future benefits of paragraph 56 (b) (withdrawal of surplus) and not to the amounts calculated in accordance with 56 (a) (contribution holidays). Each sentence in paragraph 59, other than the last sentence, specifically refers to a withdrawal of assets from the plan.

Legally speaking, and consistent with the plan text of OPSEUPP, a contribution holiday is not the same as a withdrawal of surplus, and the concepts are not interchangeable. Therefore it would not be appropriate to analogize guidance that is specific the legal circumstances surrounding surplus withdrawals to contribution holidays.

The last sentence in paragraph 59 refers to changes in the allocation of surplus. OTPP and OPSEUPP existing plan documents govern the allocation of surplus or establish a process governing how to agree upon the allocation of surplus on an equitable basis. In the case of OTPP, the Partners' Agreement and Funding Management Policy provide a clear process governing surplus utilization that begins with the identification of a surplus in a preliminary valuation and extends through good faith bargaining, mediation and final and binding arbitration. There is no need to change the existing rights within the contractual arrangement in order for the Ontario Provincial Government, as joint sponsor, to negotiate an expected future benefit. In the case of OPSEUPP, the surplus is currently allocated to each joint sponsor the form of their respective stabilization reserve pools. Consistent with this last sentence of paragraph 59, a change to the plan documents would be needed to alter these arrangements and any change would affect the accounting only when it became effective.

PS 3250 paragraph 52 notes that the expected future benefits may be affected if a government is not entitled to benefit fully from those expected future benefits or there are uncertainties as to the legal right to use a plan surplus. Such limitations might occur when there is an enduring promise from an employer requiring that it will always match the members' contributions, or contribute a specified dollar amount, or where there is a floor in contribution requirements, which might limit the employer's ability to benefit fully from future reductions in contributions.

In the OTPP there is no such restriction. The government's contribution required by the *Teachers' Pension Act* is limited to a maximum (and not a minimum) of the members' contributions. The current arrangement that the employers match a prior years' contribution level by members is by agreement of the joint sponsors and may be changed in the future as part of the negotiations to create an actuarially balanced funding valuation. Under the existing Plan framework, the plan sponsors' contributions can be reduced or eliminated through the exercise of shared control with the other joint sponsor.

Similarly, for OPSEUPP the plan text agrees to matching employer/member contributions, but this may also be changed through a decision by a sponsor to utilize its RSF to reduce its special payments or normal cost contributions. Contributions would also still be matched if both employer and employee contributions were reduced.

Ultimately, all the decisions regarding plan contributions and plan benefits rest with the joint sponsors, which entitle them to share any plan surplus on an equitable basis (see Section [x – recognition 2] above) and there are no legal uncertainties regarding the sponsors' rights, as joint sponsors, to determine contribution and benefit levels. It is clearly laid out in the legal and contractual arrangements of both OTPP and OPSEUPP.

Panel View

A joint sponsor does not require a unilateral legally enforceable right to reduce future contributions at the balance sheet date to have an expected future benefit under paragraph 56 (a). Rather, the sponsors jointly must be entitled under existing plan arrangements to reduce contributions. In the case of OTPP and OPSEU they do.

2) Calculation of the present value of expected future accruals for service for the current number of active employees

PS 3250 provides guidance on how to calculate the present value of expected future accruals for service for the current number of active employees.

Under this guidance, this amount is determined on a basis consistent with the accrued benefit obligation. The calculation is based on an open group, which assumes that the current number of employees will exist in perpetuity. This is generally recognized in practice as being an appropriate assumption for the application of this test under PSAS, unless a significant change in the number of members is expected, for example because a plan is closed to new members or because of a planned restructuring. The Panel is not aware of any such changes that are expected for either OTPP or OPSEUPP.

The guidance notes, that in addition to the expected future accrual for service, the expected administrative and investment expenses to be paid out of the plan can be included in the calculation, if they are not already taken into account in the expected return of assets rate.

Panel View

The application of the guidance on expected future accruals for service is relatively straightforward to apply to OTPP and OPSEUPP. The Panel suggests that the Ontario Provincial Government might consider to what extent the expenses paid out of the plans should be included in the determination of the economic benefit.

3) What are the "minimum contributions the government is required to make regardless of any surplus"

In calculating the expected future benefit that can be obtained through contribution holidays, PS 3250 requires that minimum contributions that the government is required to make regardless of any surplus are considered. If any requirements exist that would compel a sponsor to continue to make contributions at a certain level, even when there are plan surpluses on funding basis, it would be impossible for the sponsor to obtain a reduction in contributions to the plan and therefore there would be no expected future benefit that could be obtained through a contribution holiday.

Consistent with the analysis in Section [x – measurement 1] the Panel concluded that the joint sponsors can take a contribution holiday since there are no external or legal restrictions on the joint sponsors to take contribution reductions.

A question arises as to whether the surplus that is contemplated in the phrase "regardless of any surplus" is an accounting surplus or a funding surplus. The Panel understands that in practice actuaries interpret this to be funding surplus and not accounting surplus, and that if any contributions are required when there is a funding surplus these would be "minimum contributions the government is required to make regardless of any surplus".

As the OTPP Partners Agreement requires that any valuation filed for regulatory purposes must be an "actuarially balanced" valuation, there is no funding surplus that arises, as any preliminary funding surplus must be dealt with through the negotiation process. A funding surplus could arise prior to the mandatory filing of the next actuarially balanced funding valuation which must occur only once every three years. However, the joint sponsors may agree to file a funding valuation every year if they choose, to rebalance the contributions, reserves, and benefits of the plan. As the joint sponsors must agree on the contribution levels and make corresponding changes to the plan if necessary, there are no "minimum contributions" that must be made, "regardless of any surplus", as there is no minimum level of contributions that must be agreed upon by the joint sponsors. Further, since the OTPP actuarial valuations must be balanced, showing no surplus or deficit, there is also no ultimate funding surplus that is anticipated by the OTPP. They can agree to any level of contributions as long as the result is actuarially balanced and so the level of surplus absolutely affects the contributions that are determined by this negotiation process. Any agreed upon contribution rates are made with regard to the Plan's funded status and cannot be said to be required "regardless of any surplus".

Similarly, for OPSEUPP the stabilization reserves act as limits on the amount of funding surplus that accrues in the plan. Whether these stabilization reserves are used to reduce contributions or are maintained as a buffer against variability on contribution rates is at the discretion of the sponsors. This is very similar to the ability that a single sponsor has to reduce contributions or maintain a reserve as a buffer for future changes in actuarial assumptions. Again, the contributions made by the joint sponsors depend upon the Plan's funded status and cannot be said to be required "regardless of any surplus".

There is also a question as to whether a joint sponsor can impose a minimum contribution requirement on the other joint sponsor because shared control means that both sponsors must agree to any change in contribution levels. Therefore, absent any agreement, the existing contribution levels are "fixed" and cannot be changed. However this view would not be consistent with the notion that the valuation allowance is being applied to the plan as a whole, with the joint sponsors able to collectively control the contribution levels under the plan arrangements, and that the joint sponsors are entitled to an equitable portion of any surplus under the basic JDBP arrangements.

Panel view

The Panel noted that the Ontario Provincial Government had considered a number of calculations regarding the expected future benefit for both OTPP and OPSEU, based on different assumptions regarding what were the minimum contributions required under each plan. For example, scenarios included no minimum contributions, minimum contributions as the agreed upon contribution until the next mandatory negotiations in three years; minimum contributions as the currently agreed upon contributions for a longer period; and minimum contributions equal to the currently agreed upon contributions until certain limitations on contributions under the Income Tax Act would be expected to become effective .

Based on the analysis of the plan arrangements for OTPP and OPSEUPP, the Panel view is that there are no "minimum contributions regardless of any surplus" for either plan.

Panel view - Measurement

In the Panel's view, the joint sponsors of both OTPP and OPSEUPP are entitled to access any surplus in the respective Plan through contribution holidays and therefore the expected future benefits should be determined as the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus.

The expected future benefits would be calculated based on the plan as a whole. In the Panel's view there are no minimum contributions that the joint sponsors are required to make, regardless of any surplus. As such, if the present value of expected future accruals for service for the current number of active employees is sufficient to support the accrued benefit asset of each Plan, calculated in accordance with PS 3250, no valuation allowance would be required. The Ontario Provincial Government would recognize its portion of the OTPP accrued benefit asset and the OPSEUPP accrued benefit asset in the Public Accounts.

The Panel noted that determining the "minimum contributions that the government is required to make regardless of any surplus" for both sole sponsored plans and JDBPs may be difficult and subject to significant interpretations, indicating that PS 3250 is not as clear as it could be regarding the application of the defined benefit plan guidance to JDBPs. Section [x] of the report includes a recommendation to the PSAB Employment Benefits Task Force on this observation.

Recommendations to PSAB Employment Future Benefits Task Force

Application of guidance to Joint Defined Benefit Plans

The Panel notes that the standard would benefit from clarification on how the ability to access expected future benefits should be applied in the context of Joint Defined Benefit Plans. A clarification on how the guidance in PS 3250.81 should be applied (Interpretation A or Interpretation B) would be helpful.

Minimum contributions

In looking at the issues in respect of the OTPP and OPSEUPP the Panel observed that funding valuations drive decision making over plan funding including contribution increases or reductions by sponsors. However, funding valuations may result in net pension assets or liability that are very different from the accounting net pension asset or liability. This results in a lack of clarity about whether minimum contributions may be required "regardless of any surplus" and whether a sponsor will be able to access an accounting surplus when the funding surplus is much smaller, or there is a funding liability. The Panel also observed that other GAAPs include additional interpretation, such as IFRIC 14, *The Limit on a Defined Benefit Asset, minimum Funding Requirements and their Interaction*, but PSAS currently contains no additional interpretation. The Panel believes it would be beneficial for the Task Force to consider whether PSAB should provide additional guidance in this area.

Additional clarity on what constitutes a “minimum contribution” could increase consistency of application of this guidance for joint defined benefit plans. There can be difficulty in determining minimum contributions in the context of JDBPs and some single sponsor plans, when future contributions are dependent on future negotiations, which in turn depend on the future funded status of the plan. For example, whether the minimum contributions are based on accounting surplus or funding surplus; or whether the determination be based only on present surplus or on a projected future surplus.

Deferral accounting

In looking at the issues in respect of the OTPP and OPSEUPP the Panel observed that the existing deferral provisions have the potential to result in an asset being recognized on financial statements when there is no underlying economic resource. Although this is not the case for either the OTPP or the OPSEUPP, this could occur when unamortized losses exist such that, despite the fair value of the plan assets being less than the estimated accrued benefit obligation, an accrued benefit asset could still be presented. This can be confusing to users of the financial statements as it is not transparent as to the underlying economic resource of the plan. Transparency is in the public interest. It is most transparent when all liabilities or assets that exist are recognized and assets are not recognized where there is no underlying resource that gives rise to future economic benefit. Any mechanisms used to deal with potential income statement volatility concerns (such as recognizing gains and losses outside of the statement of operations) should ensure that these do not result in lack of transparency on the balance sheet.

Discount rates

The Panel supports PSAB examining discount rates for employment benefits. The Panel understand that in the public sector the sponsor’s borrowing rate is often used for unfunded plans and an asset return rate is used for funded plans. An appropriate asset return rate will vary depending on how the assets are invested. The discount rates used by public sector entities is also likely to be different than the discount rates used in a plan’s own financial statements prepared under Part IV of the CPA Canada Handbook – Accounting, resulting in significantly different measurements of accrued benefit obligations for the same plan in different financial statements. This lack of consistency is confusing to users.

The Panel observes that many more recent accounting pronouncements relating to liability measurement require that the discount rate used to measure the liability capture the risks inherent in that liability. The Panel suggests that the Task Force consider whether the method intended to be used to settle an obligation should affect how that obligation is measured and how the risks inherent in the obligation are best captured either in the discount rate or in other aspects of the measurement of the obligation.

Funding valuation

As a funding valuation may result in a funding surplus or deficit that is very different from the accounting surplus or deficit this may be confusing to some users where both measures are presented in the same document.

The Panel believes it may be beneficial to include additional discussion in a revised standard or other material about how the objectives and assumptions in funding valuations may differ from those used in the accounting valuation and why.

The Panel suggests that a disclosure highlighting differences in the funding valuation compared to the accounting valuation should be made in the financial statements of pension plans and/or in the financial statements of sponsors when information on the funding valuation of a plan is also made public or available to the same users of the financial statements. This would be useful to users as it would provide additional context for both the accounting and funding valuations.

Appendix A – Pension Plan Governing Arrangements

OTPP

- The *Teachers' Pension Act*, R.S.O. 1990, c.T.1 (Link to the Teachers' Pension Act);
- The *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 and the regulations thereunder (Link to the Pension Benefits Act);
- The plan text for OTPP;
- An agreement between Her Majesty the Queen in right of the Province of Ontario represented by the Minister of Education and Training and The Ontario Teachers' Federation represented by its Executive, dated July 15, 1991, as amended (The Partners' Agreement);
- A Funding Management Policy, attached as Appendix A to the Partners' Agreement (FMP).

OPSEU

- The Ontario Public Service Employees' Union Pension Act, 1994 S.O. 1994, c 17, s.143 Sched (Link to the Ontario Public Service Employees' Union Pension Act)
- The *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 and the regulations thereunder (Link to the Pension Benefits Act);
- The sponsorship agreement between Her Majesty the Queen in right of the Province of Ontario represented by the Chair of the Management Board of Cabinet and the Ontario Public Service Employees' Union, dated April 18, 1994, as amended (The Sponsorship Agreement);
- The Agreement and Declaration of Trust of OPSEU Pension Plan Trust Fund, dated October 25, 1994, as amended (The Trust Agreement);
- The plan text for OPSEUPP;
- OPTrust Funding policy.

Appendix B - Accounting references

Canadian Public Sector Accounting Standards

PS 1000, Financial Statement Concepts

PS 1000.13 Context of government financial statements

.13 Nevertheless, financial statements are a central feature of government financial reporting. They serve as a means by which a government provides an accounting of its administration of public financial affairs and resources. These financial statements are a principal means of communicating financial information to those not involved in the government's financial administration and present aggregated information capable of integration with other financial statements, schedules and reports provided by the government. Because of this key role, the objectives of government financial statements (see FINANCIAL STATEMENT OBJECTIVES, Section PS 1100) are a significant factor in the selection of accounting policies used in government financial reporting and in the determination of information required from the accounting system.

PS 1000.23 -.31 Qualitative Characteristics

.23 The function of financial statements is the communication of information to users. To fulfill this function effectively, the information must be relevant and reliable, and communicated in a manner that best facilitates its use.

.24 Financial statements should communicate information that is relevant to the needs of those for whom the statements are prepared, reliable, comparable, understandable and clearly presented in a manner that maximizes its usefulness.

.25 Financial statements provide evidence of accountability and report information required by users to help them make assessments and judgments concerning government financial operations and management. To adequately serve these needs in a manner that maximizes its usefulness, information in financial statements must possess certain basic qualities. These qualities are essential to the utility of government financial statements. The information required to meet the objectives of government financial statements needs to embody these essential characteristics.

Relevance

.26 For the information provided in financial statements to be useful, it must be relevant to the decisions made by users and for assessing accountability. Information is relevant by its nature when it can influence the decisions of users by helping them evaluate the financial impact or potential financial impact of past, present or future transactions and events or confirm, or correct, previous evaluations. For the information in government financial statements to be relevant to the needs of users, it must also be of a nature, and presented in a manner, that helps users assess the accountability of the government for its administration of public resources and financial affairs.

.27 Financial statements are not intended to provide all of the information necessary to users for decision making or for assessing government accountability. Nevertheless, they provide a fundamental component of the information needed for such purposes.

.28 Relevance is achieved through information that has predictive, feedback and accountability value, and is timely.

(a) **Predictive value and feedback value**

Information that helps users to predict a government's future financial results and cash flows has predictive value. Although the data provided in financial statements will not normally be a prediction in itself, it may be useful in making predictions. The predictive value of the statement of operations, for example, is enhanced if abnormal items are separately disclosed. Information that confirms or corrects previous predictions has feedback value. Information often has both predictive value and feedback value.

(b) **Accountability value**

Information that helps users assess a government's stewardship of the resources entrusted to it, including how resources have been applied and consumed in providing services, has accountability value. Information in government financial statements must be presented in a manner that assists in discharging this accountability. To provide accountability value, financial statements should reflect the nature and dimensions of financial position and performance that are characteristic of and appropriate to the unique nature of government. Accountability value is enhanced when financial statements identify the financial objectives and targets normally established by formal process and measure actual achievements against those financial objectives and targets. The accountability value of the information in the financial statements is also enhanced when the financial and non-financial performance information disclosed elsewhere in the Public Accounts, annual report or other report of the government can be related to the information in financial statements.

(c) **Timeliness**

Information should be timely. Financial statements issued long after the end of the fiscal period are of historical interest only. For information to be useful for decision making and accountability, the decision maker or stakeholder must receive it before it loses its capacity to influence decisions. The usefulness of information for decision making and assessing accountability declines as time elapses.

Reliability

.29 Information should be reliable. Inaccurate, inappropriate or incomplete information, or information that is biased or does not faithfully represent what it purports to represent, will inhibit rather than enhance understanding, evaluation and decision making by users and adversely affect the accountability provided by the financial statements to stakeholders. Reliable information has the following characteristics.

(a) **Representational faithfulness**

Representational faithfulness is achieved when transactions and events affecting the entity are presented in financial statements in a manner that is in agreement with the actual underlying transactions and events. Thus, transactions and events are accounted for and presented in a manner that conveys their substance rather than necessarily their legal or other form. The substance of transactions and events may not always be consistent with that apparent from their legal or other form. To determine the substance of a transaction or event, it may be necessary to consider a group of related knowledgeable and independent observers would concur that it is in agreement with the actual underlying transaction or event with a reasonable degree of precision.

(b) **Completeness**

Information is complete when none of the data necessary to achieve representational faithfulness is lacking. Completeness of disclosure means providing sufficient information about transactions, circumstances or events of such size, nature or incidence that their disclosure is necessary to understand the government's finances. In assessing the degree of completeness of the information provided in financial statements, the benefit / cost constraint in paragraph PS 1000.22 and the qualitative characteristics trade-off described in paragraph PS 1000.32 would be considered. Reliability implies completeness of information, at least within the bounds of what is material and feasible, considering the cost. An omission can rob information of its claim to neutrality if the omission is material and is intended to induce or inhibit some particular mode of behaviour.

(c) **Neutrality**

Information is neutral when it is free from bias that would lead users towards making decisions that are influenced by the way the information is measured or presented. Bias in measurement occurs when a measure tends to consistently overstate or understate the items being measured. In the selection of accounting principles, bias may occur when the selection is made with the interests of particular users or with particular economic or political objectives in mind. Financial statements that do not include everything necessary for faithful representation of transactions and events affecting the entity would be incomplete and, therefore, potentially biased.

Neutrality does not mean "without purpose", nor does it mean that accounting should be without influence on human behaviour. Accounting information cannot avoid affecting behaviour, nor should it. It is, above all, the predetermination of a desired result, and the consequential selection of information to induce that result, that negates neutrality in accounting. To be neutral, accounting information must report economic activity as faithfully as possible, without colouring the image it communicates for the purpose of influencing behaviour in some particular direction.

(d) **Conservatism**

The application of conservatism in making judgments under conditions of uncertainty affects the neutrality of financial statements in an acceptable manner. When uncertainty exists, estimates of a conservative nature attempt to ensure that assets, revenues and gains are not overstated and, conversely, that liabilities, expenses and losses are not understated. Conservatism does not, however, encompass the deliberate understatement of assets and revenues or the deliberate overstatement of liabilities and expenses.

(e) **Verifiability**

The financial statement representation of a transaction or event is verifiable if knowledgeable and independent observers would concur that it is in agreement with the actual underlying transaction or event with a reasonable degree of precision. Verifiability focuses on the correct application of a basis of measurement rather than its appropriateness.

Comparability

.30 Comparability is a characteristic of the relationship between two pieces of information rather than of a particular piece of information by itself. It enables users to identify similarities in and differences between the information provided by two sets of financial statements. Uniformity in application of principles is important when comparing the financial statements of two different entities. Consistency in application is important when comparing the financial statements of the same entity over two periods or at two different points in time. Consistency helps prevent misconceptions that might result from the application of different accounting policies in different periods. When a change in accounting policy is deemed to be appropriate, disclosure of the effects of the change is necessary to maintain comparability.

Understandability and clear presentation

.31 Information should be understandable and clearly presented. Excessive detail, vague or overly technical descriptions, and complex presentation formats result in confusion and misinterpretation. Users need information presented clearly and simply. For the information provided in financial statements to be useful, it must be capable of being understood by users. Users are assumed to have a reasonable understanding of economic activities and accounting, together with a willingness to study the information with reasonable diligence.

PS 1000.35-38 Definition of an asset [Currently effective, prior to adoption of PS 3210, Assets]

.35 **Assets** are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

.36 Assets have three essential characteristics:

(a) they embody a future benefit that involves a capacity, singly or in combination with other assets, to provide future net cash flows, or to provide goods and services;

(b) the government can control access to the benefit; and

(c) the transaction or event giving rise to the government's control of the benefit has already occurred.

.37 An item is not an asset of a government if it lacks one or more of the essential characteristics listed in the preceding paragraph. Thus, for example, an item does not qualify as an asset of a government if the item involves:

(a) no future economic benefit;

(b) future economic benefit, but the government cannot obtain it; or

(c) future economic benefit that the government may obtain, but the events or circumstances that give the government control of the benefit have not yet occurred.

.38 For an asset to be a government's asset, that government must control the future economic benefit associated with the asset to the extent that it can benefit directly from the asset and generally can deny or regulate access to that benefit by others. For example, the direct benefits of education and health care programs accrue to and are controlled by the individuals who are educated or treated and healed. Therefore, the costs of such programs, which are often called "investments", are excluded from being assets of the government.

PS 1000.52-.56 Recognition

.52 Recognition is the process of including an item in the financial statements of an entity. Recognition consists of the addition of the amount involved into item totals on a financial statement together with a narrative description of the item (for example, receivables, user fees, grants) in a statement. Similar items may be grouped together in the financial statements for the purpose of presentation.

.53 Recognition means inclusion of an item within one or more individual statements and does not mean disclosure in the notes to the financial statements. Notes either provide further details about items recognized in the financial statements, or provide information about items that do not meet the criteria for recognition and thus are not recognized in the financial statements.

.54 The recognition criteria below provide general guidance on when an item is recognized in the financial statements. Whether a particular item is recognized or not will require the application of professional judgment in considering whether the specific circumstances meet the recognition criteria.

.55 The recognition criteria are as follows:

(a) the item has an appropriate basis of measurement, and a reasonable estimate can be made of the amount involved; and

(b) for an item that involves obtaining or giving up future economic benefits, it is expected that such benefits will be obtained or given up.

.56 It is possible that an item will meet the definition of an element but still not be recognized in the financial statements because it is not expected that future economic benefits will be obtained or given up or because a reasonable estimate cannot be made of the amount involved. It may be appropriate to provide information about items that do not meet the recognition criteria in notes to the financial statements. "Expected" is used with its usual general meaning and refers to that which can reasonably be anticipated, contemplated or believed on the basis of available evidence or logic but is neither certain nor proved. The use of the word in the recognition criteria is intended to acknowledge that economic activities occur in an environment characterized by uncertainty. It is not intended to accommodate the recognition of items that do not meet the definition of one of the elements of financial statements. By implication, recognition would, therefore, not be appropriate without the occurrence of a past transaction or economic event that gives rise to an asset, liability, revenue or expense as defined in this Section.

PS 1100, Financial Statement Objectives

PS 1100.19-.32, Reporting financial position [Currently effective, prior to adoption of PS 3210, Assets]

.19 Financial statement information is used to gain an understanding of, and assess the state of, a government's finances at a point in time. Such information facilitates assessments of the government's financial viability, future tax and revenue requirements, and ability to maintain and expand the level and quality of its services.

.20 **Objective 2**

Financial statements should present information to describe the government's financial position at the end of the accounting period. Such information should be useful in evaluating:

(a) the government's ability to finance its activities and to meet its liabilities and contractual obligations; and

(b) the government's ability to provide future services.

.21 Governments provide public services and redistribute wealth for a variety of social and economic purposes. To meet those objectives, governments need information about the cost of services and the affordability of services. An understanding of the extent of the financial "lien" the government has on its ability to provide future services as a result of past transactions and events is essential information. Governments also need to have an appreciation of the magnitude of the total economic resources they have on hand to deliver services. A government's net financial resources / net debt position, assessed in combination with the non-financial resources position of the government, provides a measure of the net recognized economic resources available to the government at the financial statement date to provide services in the future.

.22 **Economic resources** are scarce means that are useful for carrying out economic activities, such as consumption, production and exchange. Financial and non-financial resources comprise the economic resources of a government.

.23 **Financial resources** include cash, claims to cash, investments and any other resources of the government that are not for consumption in the normal course of operations and are expected to contribute to net cash inflows (such as inventories for resale). A government's financial assets, as defined in FINANCIAL STATEMENT CONCEPTS, Section PS 1000, comprise the financial resources of a government.

.24 **Non-financial resources** include all items of a fixed or permanent nature (such as tangible capital property), claims to goods and services (such as prepaid items) and consumable goods (such as inventories of supplies). Non-financial resources also include intangibles, Crown lands and natural resources.

.25 Certain non-financial resources are, however, not given accounting recognition as assets in government financial statements. For example, all government intangibles, and all natural resources and Crown lands that have not been purchased by the government, are not given accounting recognition in government financial statements. A government's non-financial assets, as defined in FINANCIAL STATEMENT CONCEPTS, Section PS 1000, comprise the recognized non-financial resources of a government.

.26 Because the non-financial resources of government are different in nature from those held by a business, however, the financial position of a government has two dimensions:

(a) the net financial resources or net debt of a government; and

(b) the recognized non-financial resources of the government, which represent unexpired service potential available to be consumed by the government in the future.

.27 The term "net debt" is used to describe the first indicator of a government's financial position in this Section. The net assets of a government represent the net economic resources recognizable by the government. The two dimensions of the government's financial position are combined to calculate this second indicator of a government's financial position, called its accumulated surplus or deficit.

.28 Net debt is measured as the difference between a government's liabilities and financial assets. This difference bears directly on the government's future revenue requirements and on its ability to finance its activities and meet its liabilities and contractual obligations. Net debt provides a measure of the future revenues required to pay for past transactions and events. The extent of a government's net debt and the financial ability of the government to service that debt is an important test of the sustainability of that government. When a government's financial assets exceed its liabilities, this indicator of a government's financial position would be called "net financial assets" and it would provide a measure of the net financial assets on hand that can provide financial resources to finance future operations.

.29 A government's net debt is an important indicator of a government's financial position, highlighting the financial affordability of future government service provision. A net debt position represents a "lien" on the ability of the government to apply financial resources and future revenues to provide services. Non-financial assets are added to net debt to calculate the other indicator of a government's financial position — its accumulated surplus or deficit. Non-financial assets are "prepaid service potential". Reporting a government's recognized non-financial resources as part of its financial position provides information necessary for a more complete understanding of a government's debt position, financial position and future operating requirements.

.30 The nature of the majority of government non-financial assets is different from the nature of those held by a business. Capital assets are held by a business in order to generate future net cash inflows to provide a return to investors, as well as to finance operations, expansion and debt retirement. If the net realizable value of an asset of a business is greater than the present value of its expected future net cash inflows to the business, it would normally be sold. In contrast, for government, like not-for-profit organizations, recognition and valuation of capital assets are based on their service potential; for the most part, such assets do not generate future net cash inflows. In addition, they do not normally provide resources to discharge the liabilities of the government, unless they are sold and thus converted back into financial assets.

.31 The tangible capital assets and other non-financial assets of a government form part of its financial position because they provide resources that the government can employ in the future to accomplish its objectives. The government can use these assets to provide services. The services that the government can provide as a result of owning a capital asset are the future benefits embodied by the asset. Including such assets in the government's financial position provides a more complete picture of the economic resources available to and utilized by the government.

.32 A key distinction between the financial and non-financial assets of a government is the degree of choice in application associated with them. Financial assets can be used to discharge liabilities or provide services, while non-financial assets can normally be used only for service provision. Given that many users are more familiar with the nature of the elements reported in the financial statements of profit-oriented enterprises, it is crucial that the financial statements identify this fundamental characteristic of government non-financial assets.

PS 1150, Generally Accepted Accounting Principles

PS 1150.04-.12 Sources of GAAP

.04 A public sector reporting entity should apply every primary source of GAAP that deals with the accounting and reporting in financial statements of transactions or events encountered by the public sector reporting entity.

.05 When the primary sources of GAAP do not deal with the accounting and reporting in financial statements of transactions or events encountered by the public sector reporting entity, or additional guidance is needed to apply a primary source to specific circumstances, the selection of an appropriate accounting policy requires the exercise of professional judgment. In these circumstances, a public sector reporting entity should adopt accounting policies and disclosures that are consistent with:

(a) the primary sources of GAAP; and

(b) the application of the concepts described in FINANCIAL STATEMENT CONCEPTS, Section PS 1000.

.06 The primary sources of GAAP provide the financial statement accounting and reporting requirements, as well as explanations and guidance for most transactions and events encountered by a public sector reporting entity. Management is required to be knowledgeable about the primary sources of GAAP. As well, management is required to be aware of changes to the primary sources, because what constitutes GAAP at a particular time changes and adapts to reflect economic and social conditions.

.07 No rule of general application can be phrased to suit all circumstances or combinations of circumstances that may arise. As a result, matters may arise that are not specifically addressed in the primary sources of GAAP. It is necessary to refer to other sources when the primary sources do not deal with the accounting and reporting in financial statements of transactions or events that a public sector reporting entity encounters, or when additional guidance is needed to apply a primary source to specific circumstances.

.08 A public sector reporting entity consults sources other than primary sources of GAAP to assist in selecting accounting policies and disclosures only when these sources comply with paragraph PS 1150.05. The public sector reporting entity evaluates sources in selecting the appropriate accounting policies and disclosures based on all of the following criteria:

(a) The specificity of the source — A source that deals with the specific circumstances is likely to be more relevant than one from which the public sector reporting entity must analogize.

(b) The authority of the issuer or author — A source issued by an accounting standard setter in its own jurisdiction is likely to be more relevant than a source issued by others in the same jurisdiction.

(c) The continued relevance of the source — The passage of time may diminish the relevance of certain sources.

(d) The development process for the source — A source developed after extensive consultation and debate is likely to be more relevant than a source developed without such discipline.

.09 The selection of appropriate accounting policies and disclosures requires the exercise of professional judgment. In exercising professional judgment, a public sector reporting entity takes into account the primary sources of GAAP, as well as the concepts described in paragraph PS 1150.05(b). The public sector reporting entity would not analogize to a primary source of GAAP if the source used states that it applies only to the particular circumstances described therein.

.10 A public sector reporting entity considers all sources of GAAP that it consults in the context of the concepts described in paragraph PS 1150.05(b), which describes the concepts underlying the development and use of accounting principles in financial statements. A public sector reporting entity adopts accounting policies that are consistent with these concepts. The Public Sector Accounting Board (the Board) considers a source to be consistent with the concepts in paragraph PS 1150.05(b) when the guidance in that source is compatible with the qualitative characteristics of financial information, the elements of financial statements, and the recognition and measurement criteria in paragraph PS 1150.05(b).

.11 In selecting appropriate accounting policies and disclosures, interpretations of a source do not constitute evidence that the criteria in paragraph PS 1150.05 have been met if it is likely that most parties, exercising professional judgment, would reject them as not resulting in a fair presentation in accordance with GAAP.

.12 When the concepts described in paragraph PS 1150.05(b) conflict with a primary source of GAAP, the requirements of the primary source of GAAP prevail. The Board is guided by the concepts described in paragraph PS 1150.05(b) in the development of future pronouncements and in its review of existing pronouncements. Therefore, the number of cases of conflicts between the concepts described in paragraph PS 1150.05(b) and primary sources of GAAP will diminish over time.

PS 1150.14 Primary sources of GAAP

.14 In CPA Canada PSA Handbook Sections, italicized and non-italicized paragraphs have equal authority. Italicized paragraphs generally state the main principles, while non-italicized paragraphs generally explain the principles or their application to a particular situation. In addition, non-italicized paragraphs may include guidance for practices that are encouraged or desirable, but not required. To be in accordance with GAAP, a public sector reporting entity needs to comply with the non-italicized paragraphs as well as the principles. When there appear to be different ways of interpreting the non-italicized paragraphs, the public sector reporting entity selects the treatment that is most consistent with the principles.

PS 1150.18-.20 Other sources

.18 Paragraphs PS 1150.19-.24 identify some of the other sources that a public sector reporting entity might consult to assist in selecting accounting policies and disclosures that comply with paragraph PS 1150.05.

.19 Pronouncements issued by other bodies authorized to issue accounting standards may be useful sources to consult. For example, accounting pronouncements published with the authority of the Canadian Accounting Standards Board (AcSB), International Accounting Standards Board (IASB), US Federal Accounting Standards Advisory Board (FASAB), US Governmental Accounting Standards Board (GASB), or International Public Sector Accounting Standards Board (IPSASB) are often important sources to consult on matters not covered by primary sources of GAAP or for assistance in applying a primary source of GAAP to specific circumstances.

.20 When a public sector reporting entity chooses to consult a source described in paragraph PS 1150.19, it applies professional judgment and evaluates the source in the context of the relative manner in which the standard setter requires its pronouncements to be applied, as well as in the context of the related pronouncement. When an accounting standard setter does not have a conceptual framework that is similar to the concepts referred to in paragraph PS 1150.05(b), the public sector reporting entity needs to ensure that the selected source is consistent with those concepts.

PS 3210, Assets [Effective for annual periods beginning on or after April 1, 2017]

PS 3210.03-.05 Assets

.03 **Assets** are economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained.

.04 Assets have three essential characteristics:

(a) They embody future economic benefits that involve a capacity, singly or in combination with other assets, to provide goods and services, to provide future cash inflows, or to reduce cash outflows.

(b) The public sector entity can control the economic resource and access to the future economic benefits.

(c) The transaction or event giving rise to the public sector entity's control has already occurred.

.05 Economic resources are not assets unless they meet the three characteristics of assets.

PS 3210.06-.10 Economic resources

.06 Economic resources embody value because they enable an entity to meet its objectives, such as the provision of public goods and services, redistribution of wealth, generation of cash inflows or reduction of cash outflows.

.07 To embody value as an economic resource, there must also be some restriction on its availability. For example, the air we breathe generally cannot be an economic resource unless access to it is restricted.

.08 Economic resources can arise from, but are not limited to, the following:

(a) contracts or agreements (for example, accounts receivable and leases);

(b) another government's legislation (for example, transfers receivable);

(c) government's own legislation (for example, taxes, fines and penalties);

(d) voluntary contributions (for example, donations); or

(e) construction and development (for example, roads).

.09 Economic resources can be:

(a) financial in nature (for example, cash, accounts receivable and investments); or

(b) non-financial in nature (for example, tangible capital property, prepaid items and inventories of supplies).

.10 Without an economic resource, future economic benefits cannot be obtained. For example, a fire truck (the economic resource) needs to exist before it can provide fire suppression services (the future economic benefits).

PS 3210.11-.15 Future economic benefits

.11 The essence of assets are their future economic benefits. Assets embody future economic benefits that allow public sector entities to achieve their objectives. The future economic benefits embodied in assets involve a capacity, singly or in combination with other assets, to provide goods and services, to provide future cash inflows or to reduce cash outflows.

.12 Often the public is the beneficiary of the goods and services provided by a public sector entity. For example, assets such as fire trucks are used to provide fire suppression services to the public. Hospital buildings and medical equipment are used to provide health care services. Parks, schools and libraries provide recreational, educational and research opportunities to the public. Water treatment plants provide goods, such as potable water. Such assets benefit public sector entities as they assist in achieving the entity's primary objective of providing public goods and services. This benefit is different from the benefit that the public receives.

.13 The future economic benefits embodied in an asset may also be in the form of generating future cash inflows. Cash inflows benefit the public sector entity because cash can be used to purchase or to provide goods and services, redistribute wealth or settle liabilities. Benefits in the form of cash inflows relate to resources, such as loans receivable, inventory for resale and portfolio investments. Also, some public sector resources generate cash inflows because they have user fees associated with them.

.14 The future economic benefits may also take the form of a capacity to reduce cash outflows. For example, this may be the case when betterment of a tangible capital asset reduces the cost of providing goods and services.

.15 There is a close association between incurring a cost and the generation of an asset. However, not all costs result in a future economic benefit. For example, costs incurred to maintain the current service capacity of an asset do not provide a future economic benefit. Also, a public sector entity may obtain an asset without incurring costs. For example, items that have been donated to the public sector entity may provide that entity with future economic benefits and, hence, satisfy the definition of assets.

PS 3210.16-.21 Control

.16 A public sector entity controls the economic resource and access to the future economic benefits when it:

(a) can benefit from the economic resource through its capacity to provide goods and services, to provide future cash inflows or to reduce cash outflows;

(b) can deny or regulate access to those benefits by others; and

(c) is exposed to the risks associated with the economic resource.

.17 An entity that controls an economic resource has the ability to benefit from the economic resource. For example, a recipient of a transfer benefits from the transfer as it can use the transfer to provide goods or services.

.18 An entity that controls an economic resource has the ability to deny or regulate access to the future economic benefits associated with the economic resource by others. For example, an entity controlling a bus has the ability to deny or regulate access to the related transportation services.

.19 An entity that controls an economic resource is exposed to the risks associated with the economic resource. For example, the entity may hold an investment, the value of which may decline and result in a loss.

.20 Some economic resources are subject to certain external restrictions that specify the purpose(s) for which resources are to be used. For example, there may be external restrictions imposed on the public sector entity's own assets, as is the case with some sinking fund investments. Such restrictions on the use of an economic resource do not negate the public sector entity's control of the economic resource.

.21 Although control may be seen as applying to an asset as a whole, the concept can also be applied to individual rights related to the asset. For example, a single leased asset embodies different economic benefits. It may give the lessee the right to use the property and the lessor the right to receive rents and any residual value. Thus, both parties may have assets corresponding to their respective rights.

PS 3250, Retirement Benefits

PS 3250.17 Components of the retirement benefit liability

.017 The components of the retirement benefit liability are:

(a) accrued benefit obligation including the effects of plan amendments, settlements and curtailments;

(b) plan assets, if any; and

(c) unamortized actuarial gains and losses.

PS 3250.50-.59 Limit on the carrying amount of an accrued benefit asset

.050 An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs.

.051 A government with a defined benefit plan may have an accrued benefit asset for accounting purposes. An accrued benefit asset arises when the government's total contributions to the plan, including interest earned thereon, are greater than the retirement benefit expense recognized since the start of the plan. Contributions reflect the funding objectives of the plan. The benefit expense reflects the accounting objectives and may differ for a number of reasons, including the fact that actuarial gains and losses are deferred and amortized in future periods.

.052 A government may benefit from an accrued benefit asset either by withdrawing surplus assets or by taking a contribution holiday or receiving a refund of contributions. The accrued benefit asset may become impaired when there is a plan surplus for accounting purposes that the government is not entitled to benefit from fully. For example, there may be a regulatory moratorium on pension surplus withdrawals or uncertainties as to a government's legal right to use a plan's accounting surplus.

.053 To determine the extent to which an accrued benefit asset may be impaired, the government first determines the adjusted benefit asset. The adjusted benefit asset is the accrued benefit asset less net unamortized actuarial losses (determined on a basis using market value of assets).

.054 The adjusted benefit asset is then compared to the expected future benefit. When the expected future benefit exceeds the adjusted benefit asset, the accrued benefit asset is not impaired and, accordingly, no valuation allowance is required. The chart included as Appendix A to this Section is intended to set out the relationship between the various defined terms.

.055 The objective of the standard in paragraph PS 3250.050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions.

.056 A government determines its expected future benefit as the sum of:

(a) the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus; and

(b) the amount of the plan surplus that can be withdrawn in accordance with the existing plan and any applicable laws and regulations.

.057 A government's expected future accruals for service for the current number of active employees are determined on a basis consistent with that used to determine its accrued benefit obligation. These expected future accruals for service, less required employee contributions and minimum contributions the government is required to make regardless of any surplus, are then discounted back to the current period to determine the present value. The interest rate used to calculate this present value is the expected rate of return on plan assets used to determine the benefit expense in the period.

.058 When administration expenses are paid by the plan and included in the normal cost calculation, a best estimate of the future administration expense is included in the expected future accruals for service. When administration expensxes are paid by the plan and not included in the normal cost calculation, the rate of return on plan assets is adjusted to reflect the deduction of the administrative expenses.

.059 A key factor in determining a government's expected future benefit from a defined benefit plan with a plan surplus for accounting purposes is the ability of the government to withdraw assets from the plan. The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal. It excludes any withdrawable plan surplus a government is currently required, or intends, to allocate to employees. A government may not anticipate obtaining a legally enforceable right to withdraw a portion of a plan surplus to which it is not currently entitled, whether on the basis of precedent or otherwise. Accordingly, when withdrawal of plan surplus requires the approval of employees or an appropriate regulatory authority or a court of law, a government excludes any amount subject to this restriction from its expected future benefit until such approval has been obtained. A change in the allocation of surplus between a government and its employees is incorporated into the calculation of the expected future benefit only when it has been agreed to and, when required, approved by the appropriate regulatory authorities.

PS 3250.79-.82 Joint defined benefit plans

.079 Governments may participate jointly in defined benefit plans where the government shares the risks and rewards jointly with plan participants, represented by a sponsor or sponsors. Joint defined benefit plans are governed by a formal agreement between the sponsors, which establishes that the sponsors have shared control over the plan. A governing board is generally appointed by the joint sponsors with equal representation and a mutually agreed-upon chair.

.080 A government would consider the characteristics of the plan to determine whether it meets the definition of a joint defined benefit plan. In a joint defined benefit plan, funding contributions are shared mutually between the government and the plan members. The sponsors have control over decisions related to the administration of the plan and the level of benefits and contributions on an ongoing basis based on the terms of the contractual agreement. The sponsors share, on an equitable basis, the significant risks associated with the benefit plan. Risk would not be considered to be equitably shared in an arrangement where the government and the joint sponsors fund the plan equally but where the government retains the full risk of the accrued benefit obligation. If the government retains the residual risks it is unlikely that the plan meets the definition of a joint defined benefit plan.

.081 When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.

.082 A government may convert an existing defined benefit plan for which it is the sole sponsor to a joint defined benefit plan where the risks and benefits are shared. When converting to a joint plan, a government would consider whether there are any special accounting issues that arise, including whether the predecessor plan has been settled or partially settled and/or curtailed or partially curtailed. In assessing such issues a government would have regard to its specific circumstances and the terms of the joint defined benefit plan.

PS 3250.GLOSSARY (select definitions)

An **accrued benefit asset** is the amount of any asset recognized on a government's statement of financial position in respect of employee retirement benefits before deducting any valuation allowance that may be required. It is the sum of the government's accumulated cash contributions less the sum of the current and prior years' benefit expenses (before any change in the valuation allowance).

An **accrued benefit obligation** is the value of retirement benefits attributed to services rendered by employees and former employees to the financial statement date.

Actuarial gains and losses are changes in the value of the accrued benefit obligation and the plan assets resulting from:

(a) experience different from that assumed; or

(b) changes in an actuarial assumption.

An **actuarial valuation for accounting purposes** is an assessment of the financial status of a benefit plan. It consists of the valuation of assets held by the plan and calculation of the actuarial present value of benefits to be paid under the plan. The valuation provides the information needed to determine the retirement benefit liability and related expenses in accordance with this Section.

An **actuarial valuation for funding purposes** is an assessment of the financial status of a benefit plan. It consists of the valuation of assets held to discharge the benefit liability and calculation of the actuarial present value of benefits to be paid under the plan. The valuation results in a calculation of the required future contributions and a determination of any gains or losses since the last valuation.

An **adjusted benefit asset** is an accrued benefit asset less the amount, if any, by which the aggregate of any unamortized actuarial losses exceeds the aggregate of any unamortized actuarial gains.

The **expected future benefit** is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions. A government determines its expected future benefit as the sum of:

(a) the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus; and

(b) the amount of the plan surplus that can be withdrawn in accordance with the existing plan and any applicable laws and regulations.

A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:

(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;

(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;

(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and

(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.

The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.

A **multiemployer plan** is a defined benefit plan to which two or more governments or government organizations contribute, usually pursuant to legislation or one or more collective bargaining agreements. The main distinguishing characteristic of a multiemployer plan is that the contributions by one participating entity are not segregated in a separate account or restricted to provide benefits only to employees of the entity and, thus may be used to provide benefits to employees of all participating entities.

A **plan asset** is an asset segregated and restricted in a trust or other legal entity separate from the reporting government to provide for retirement benefits under the following conditions:

(a) the assets in the separate entity are to be used only to settle the related accrued benefit obligation, are not available to the government's own creditors, and either cannot be returned to the government or can be returned to the government only if the remaining assets of the trust are sufficient to meet the plan's obligations; and

(b) to the extent that sufficient assets are in the separate entity, the government will have no obligation to pay the related retirement benefits directly.

For purposes of this Section, plan assets do not include amounts held by the government and not yet paid into the trust or other legal entity.

The **retirement benefit liability** is the amount of any liability recognized on a government's statement of financial position in respect of retirement benefits. It is the sum of the current and prior years' benefits expenses less the government's accumulated cash contributions.

International Public Sector Accounting Standards

IPSASB 39, Employee Benefits

IPSASB 39.67

A net defined benefit asset may arise where a defined benefit plan has been overfunded or where actuarial gains have arisen. An entity recognizes a net defined benefit asset in such cases because:

(a) The entity controls a resource, which is the ability to use the surplus to generate future benefits;

(b) That control is a result of past events (contributions paid by the entity and service rendered by the employee); and

(c) Future economic benefits are available to the entity in the form of a reduction in future contributions or a cash refund, either directly to the entity or indirectly to another plan in deficit. The asset ceiling is the present value of those future benefits