

Osler opinion re_ OTPP surplus.rtf

From: Rienzo, Douglas [DRienzo@osler.com]
To: Hatzis, Len (TBS) [Len.Hatzis@ontario.ca]; Kaufman, Paul (TBS) [Paul.Kaufman@ontario.ca]
CC: Steele, Jana [JSteele@osler.com]; Marin, Jon [jomarin@osler.com]
Subject: Osler opinion re: OTPP surplus
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Attachment 1: image001.gif
Attachment 2: image002.gif
Attachment 3: image003.jpg
Attachment 4: Opinion dated September 20, 2016.pdf

Len, Paul:

Please find enclosed our opinion in final form. We would be pleased to discuss it with you at your convenience.

Doug Rienzo

Douglas Rienzo
Partner, Pensions & Benefits

Chair, Diversity Committee

416.862.5683

DIRECT

416.862.6666

FACSIMILE

drienzo@osler.com

Osler, Hoskin & Harcourt LLP
Box 50, 1 First Canadian Place
Toronto, Ontario, Canada M5X 1B8

<http://www.osler.com/>

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Jana Steele
Direct Dial: 416.862.6625
jsteele@osler.com

Douglas Rienzo
Direct Dial: 416.862.5683
drienzo@osler.com

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Len Hatzis
Deputy Director, Treasury Board Secretariat Legal Services
Ferguson Block
77 Wellesley Street West
9th Floor
Toronto, ON M7A 1N3

Paul Kaufman
Counsel, Treasury Board Secretariat Legal Services
Ferguson Block
77 Wellesley Street West
9th Floor
Toronto, ON M7A 1N3

Dear Sirs:

Accounting Treatment of Surplus in the Ontario Teachers' Pension Plan

I. BACKGROUND

We understand the pertinent background facts to be the following:

1. The Ontario Teachers' Pension Plan (the "**OTPP**") is a jointly-sponsored defined benefit pension plan established under the *Teachers' Pension Act* (Ontario) and is, subject to certain exceptions, required to comply with the *Pension Benefits Act* (Ontario) as well as the *Income Tax Act* (Canada).
2. The sponsors of the OTPP are the Province of Ontario (the "**Province**") and the Ontario Teachers' Federation (the "**OTF**") (collectively, the "**Sponsors**").

3. We understand that as at March 31, 2016 the Province's Statement of Financial Position (the "**Public Accounts**") includes a pension asset totalling \$10.6 billion (the "**Pension Asset**") related in part to an accounting surplus under the OTPP.¹
4. The Office of the Auditor General has indicated that because the Province does not have the legally enforceable right to unilaterally access the assets of the plan, and in the absence of that right, because the Province does not have an agreement in place with the OTF as of March 31, 2016 with respect to how the surplus would be utilized such that it would provide a benefit to the Province, the Pension Asset as presented in the Public Accounts should be removed.²

You asked us to consider the processes pursuant to which the Province may utilize surplus assets in the OTPP in accordance with the Plan Documentation (as defined below), and to identify any considerations that might inform the expectations of the Province as a Sponsor regarding the basis upon which decisions will be made relating to surplus utilization. We are not providing an opinion on the proper application of the accounting standards to the present situation, as that is an issue for the accountants to address.

II. SCOPE OF OPINION

For the purposes of our opinion, we considered the following documentation (collectively, the "**Plan Documentation**"):

1. The Ontario Teachers' Pension Plan (the "**OTPP**" or "**plan**");
2. The 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 (the "**Partners' Agreement**");
3. The Funding Management Policy (the "**FMP**"), which forms Appendix "A" to the Partners' Agreement; and
4. The Term Sheet agreed to by the Sponsors dated March 13, 2013 (the "**2013 Term Sheet**") describing the implications of the Freeze Period (as defined below) on the FMP.

¹ See letter from Bonnie Lysyk (Auditor General) to Greg Orenszak (Deputy Minister, Treasury Board) and Scott Thompson (Deputy Minister, Ministry of Finance), dated September 13, 2016. Part of the surplus relates to another pension plan; we understand that \$10.1 billion relates to the OTPP.

² *Ibid.*

We have also considered the following legislation/regulations:

1. The *Teachers' Pension Act* (Ontario) (the "**Teachers' Act**"); and
2. The *Pension Benefits Act* (Ontario) (the "**PBA**") and the regulations thereunder (the "**PBR**").

As per your instructions, we have not evaluated the ability of the Province to benefit from the *withdrawal* of surplus assets from the OTPP (although certain provisions of the FMP cited herein relate to both the withdrawal and other utilization of surplus). Rather, this opinion identifies the processes pursuant to which the Province may receive a financial benefit through the *utilization* of OTPP surplus (e.g., as a result of either a temporary reduction in the Province's contribution obligations (a contribution holiday) or through changes to the contribution formula that reduce the Province's contribution obligations).

We note that the concept of an *accounting* surplus is distinct from surplus identified in a funding valuation prepared in respect of the OTPP (a "**Funding Valuation**"). Where surplus has been identified in a Funding Valuation, the Plan Documentation provides the Sponsors with certain avenues pursuant to which the Funding Valuation surplus can be utilized. Any reference to "surplus" in this opinion, unless expressly stated otherwise, relates to the surplus identified by the actuary for the OTPP in a Funding Valuation and not to the accounting surplus identified in the Public Accounts. We understand that pursuant to the applicable accounting standards, the recognition of part or all of the accounting surplus on the Public Accounts depends on the ability of the Province to benefit from any surplus in the pension fund over the life of plan.

This opinion does not purport to draw any conclusions, express or implied, about the application of the accounting standards to the present circumstances; rather, it is solely intended to provide the Province with information concerning the legal framework governing the utilization of surplus under the OTPP so as to allow the Province's accountants to determine whether a related Pension Asset should appear on the Public Accounts.

III. SUMMARY OF OUR CONCLUSIONS

A brief summary of our material conclusions is set forth below (all capitalized terms are defined herein):

1. Paragraph 10(1)3 of the Teachers' Act provides that the Minister of Education and the executive of the OTF may enter into an agreement that provides for certain matters, including: "3. The sharing of entitlement to gains or surplus under the plan and of liability for deficiencies in the pension fund by the Minister, the employers who contribute under the plan and the active plan members". This is a

fundamental legislative pronouncement that the Province and the members of the plan are meant to “share” both upside (surplus) and downside (deficit) under the plan. Although it is not an express statement of 50/50 sharing, it would presumably inform the expectations of the Sponsors regarding how any surpluses are to be utilized. We note that the Sponsors have in fact entered into such an agreement, in the form of the Partners’ Agreement (to which is appended the FMP).

2. The Plan Documentation (specifically the FMP) and applicable legislation allow for the Sponsors to utilize surplus in a variety of ways, depending on the funded status of the OTPP. These surplus utilization options include the following avenues through which the Province may receive a financial benefit through the utilization of surplus (the three “zones” describe different levels of surplus, a greater amount of surplus being required in order for the next “zone” to come into play):
 - a. In the Restoration Zone, a Restoration Contribution Reduction may be approved once certain other requisite conditions have been met.
 - b. In the Temporary Improvement Zone, surplus may be utilized to provide a temporary contribution reduction (i.e., a contribution holiday), either as a stand-alone measure or in combination with other surplus utilization options (i.e., benefit improvements or surplus withdrawal).
 - c. In the Permanent Improvement Zone, surplus may be utilized to permanently reduce the current contribution obligations of the employers and the members, either as a stand-alone measure or in combination with changes to benefits.

Notwithstanding the foregoing, under the FMP the Sponsors have the discretion to, by mutual agreement, utilize surplus in any other manner.

3. Any enforceable legal right to obtain some value from any surplus pursuant to the Partners’ Agreement (and FMP appended thereto) would be grounded in the law of contract. As the relevant provisions of the FMP require the Sponsors to agree upon the manner in which surplus is to be utilized, neither Sponsor has a legally enforceable right to unilaterally utilize surplus in the OTPP. As such, the provisions in the FMP that contemplate the ability for the Province to receive a financial benefit through the utilization of surplus would not, in and of themselves, give rise to a legally enforceable right. What the Province does have, however, is a right to negotiate with the OTF the use of surplus that may arise under the plan, at least in the context of an actuarial valuation that discloses surplus and that is to be filed with the regulators.

4. Notwithstanding the foregoing, the Plan Documentation and applicable legislation give rise to the following considerations which may shape the Sponsors' expectation as to the basis upon which surplus will be utilized (and potentially lead to an expectation of equal sharing of the benefit of any surplus, at least over time):
 - a. The Teachers' Act prohibits the total amount of the contributions payable by the Province (and other participating employers) to exceed the amount of contributions paid by or on behalf of active members in respect of credited service for the year (subject to certain exceptions for payment of a solvency deficiency and where there are insufficient cash and liquid assets in the fund).³ In practice, this has resulted in 50/50 sharing of the regular contribution costs between the participating employers (including the Province) and plan members since the OTPP became jointly sponsored.⁴
 - b. The history of surplus utilization after the OTPP became a jointly-sponsored plan and prior to the date that the FMP was established demonstrates a past practice of the Sponsors equally sharing (in the aggregate) the financial benefits of surplus utilization, although surplus was not shared equally each time. Since the time the FMP was established, the OTPP has not reached the requisite level of surplus such that the Sponsors could negotiate its utilization under the Temporary Improvement Zone or Permanent Improvement Zone.
 - c. The inability for either party to unilaterally require surplus to be utilized in a particular manner (subject to the OTF Call Right), and the requirement to negotiate and agree (or in the absence of agreement, arbitrate) presents the Sponsors with an equal opportunity to benefit from surplus utilization.
 - d. One could argue that the obligation to bargain in "good faith" found in the Partners' Agreement may include the obligation to take into account the

³ Teachers' Act, subsections 5(1.1), (3) and (7).

⁴ We note that for the period from January 1, 2008 to December 31, 2008, the employee contribution rate was slightly lower than the employer contribution rate for earnings both above and below the Year's Maximum Pensionable Earnings ("YMPE") (9.6%/11.2% versus 10.4%/12%, respectively). It is our understanding that member contribution rates in 2008 were partially subsidized by the OTF with a credit reserve from the 1998 to 2001 pension negotiations, which accounts for this difference. See, Ontario Teachers' Pension Plan: "How Contribution Rates Have Evolved" available at: <https://www.otpp.com/documents/10179/20940/-/5e471c2b-23f1-44e6-b5c1-d22e3e50dbc3/How+Contribution+Rates+Have+Evolved.pdf>

“sharing” principles described elsewhere in this opinion, given that the OTPP is a jointly-sponsored plan.

We note that it is our understanding that it is certainly the Province’s expectation that the benefit of any surplus under the plan will in fact be shared equally between the Province and the members, over time.

5. In the event that the Sponsors cannot agree upon how surplus is to be utilized in the Restoration Zone, the Temporary Improvement Zone or the Permanent Improvement Zone, the matter can be submitted to an arbitration board of three arbitrators. Arbitration provisions are generally procedural in nature and therefore do not provide a strong foundation upon which to base parties’ reasonable expectations about their substantive rights under an agreement. To resolve a dispute, the arbitration board would engage in an exercise in interpretation of the operative substantive provisions of the relevant governing documents, including any applicable statutory provisions. However, the arbitral award must meet certain mandatory conditions set forth in the Partners’ Agreement. Among other things, the arbitral award is required to ensure that the contributions of the Minister and those employers who are required to contribute are equal to the contributions of members (section 92(c) of the Partners’ Agreement).

As part of the arbitration board’s interpretation exercise of the relevant governing documents, in the event of ambiguity in the written terms of the documents, evidence of the parties’ post-agreement practices can be admitted as an aid to interpreting the agreement. Past practices may illustrate the parties’ intentions at the time of the agreement. These considerations of past practices would be in conjunction with any explicit mandatory considerations set out in the governing document, e.g. prevailing economic conditions and the overall state of the provincial economy under section 91 of the Partners’ Agreement. The past practices which the arbitrator may consider would include those described herein: the long history of 50/50 member/employer contributions to the plan, and the equal sharing of surpluses prior to 2003 (from 2003 onwards the plan was mostly in deficit, with surpluses used to restore foregone escalated adjustments for members).

IV. FRAMEWORK IN THE PLAN DOCUMENTATION FOR SURPLUS UTILIZATION BY THE SPONSORS

1. Joint Sponsorship Plan Design and Cost Sharing

The OTPP qualifies as a “jointly sponsored pension plan” (“JSPP”) under the PBA, which has three material implications relevant to the present analysis:

1. Plan Governance – Under a JSPP, the employers (or any persons or entities who make contributions on behalf of the employers or represent the employers) and the members of the pension plan (or any representatives of the members) are jointly responsible for making all decisions about the terms and conditions of the pension plan and any amendments to the pension plan.⁵
2. Funding – The OTPP (and certain other prescribed JSPPs) are exempt from solvency funding requirements under the PBR.⁶
3. Cost Sharing – In a defined benefit pension plan which does not qualify as a JSPP, the employer is solely responsible for funding any going concern unfunded liability or solvency deficiency. Given that the OTPP qualifies as a JSPP, however, the PBA permits members to be required to make contributions in respect of any going concern unfunded liability or solvency deficiency.⁷

With respect to the cost-sharing principle referred to in #3 above, the Teachers' Act contains limitations on the contributions that the Province (and other participating employers) may make under the OTPP:

5(1.1) The total amount of the contributions payable by the Minister of Education and the employers who contribute under the pension plan in respect of any year shall not exceed the amount of contributions payable by or on behalf of active plan members in respect of credited service for that year.

Despite this general principle, under the Teachers' Act the Province is required to make additional contributions to the OTPP fund in the event that there are insufficient assets to make required payments out of the fund in any particular year.⁸ The Province is also permitted to make additional contributions in respect of a solvency deficiency⁹ (although, as noted above, solvency funding is not required under the OTPP). Notwithstanding that subsection 5(1.1) of the OTPP provides a *cap* on the Province's normal cost contribution obligation, rather than requiring 50/50 cost sharing, we understand that in practice there has been 50/50 cost sharing of the normal contribution cost under the OTPP since the OTPP became jointly sponsored (and for the majority of periods of time since the

⁵ PBR, subsection 3.1(1).

⁶ PBR, subsection 1.3.1(3).

⁷ See PBA, subsection 1(2) and subsection 55(4).

⁸ Teachers' Act, subsection 5(3).

⁹ Teachers' Act, subsection 5(7).

inception of the plan in 1917).¹⁰ The plan text itself also provides for equal contributions, at the basic level (see sections 25(1) and 26(1)).

Currently, the Sponsors are also required to mutually agree upon how any plan deficits are to be addressed.¹¹ While not binding upon the Sponsors, the FMP indicates that deficits may be addressed through increases to the contribution rates, lowering the amount of indexation and/or other decreases in benefits.

Joint governance and cost sharing form two of the core features of the OTPP. Consistent with the equal sharing of risk permitted under the JSPP plan design, there is a requirement for decisions relating to plan design and plan amendments to be made jointly by the Sponsors. In this regard, the FMP requires the Sponsors to negotiate and agree upon decisions relating to surplus utilization. Accordingly, the Sponsors can be said to have equal *opportunity* to benefit from surplus utilization through the negotiation process.

2. Provisions in the Legislation and Plan Documentation Relating to the Utilization of Surplus

(a) *Pension Benefits Act*

While they do address surplus withdrawals (which are not addressed in this opinion), the PBA and PBR do not otherwise mandate any particular use of ongoing surplus that may arise in a pension plan, e.g. for benefit improvements or contribution holidays. One must therefore look to the Teachers' Act, and to the Partners' Agreement and FMP in order to determine how ongoing surplus is dealt with under the OTPP.

(b) *Teachers' Pension Act (Ontario)*

Paragraph 10(1)3 of the Teachers' Act provides that the Minister of Education and the executive of the OTF may enter into an agreement (i.e., the Partners' Agreement) that provides for certain matters, including: "3. The sharing of entitlement to gains or surplus under the plan and of liability for deficiencies in the pension fund by the Minister, the employers who contribute under the plan and the active plan members". This is a

¹⁰ See, Ontario Teachers' Pension Plan: "How Contribution Rates Have Evolved" available at: <https://www.otpp.com/documents/10179/20940/-/5e471c2b-23f1-44e6-b5c1-d22e3e50dbc3/How+Contribution+Rates+Have+Evolved.pdf> As noted above, for the period from January 1, 2008 to December 31, 2008 the employee contribution rate was slightly lower than the employer contribution rate for earnings both above and below the YMPE (9.6%/11.2% versus 10.4%/12%, respectively). It is our understanding that member contribution rates in 2008 were partially subsidized by the OTF with a credit reserve from the 1998 to 2001 pension negotiations, which accounts for this difference.

¹¹ See, for example, Section 3.09 and 3.11 of the FMP.

fundamental legislative pronouncement that the Province and the members of the plan are meant to “share” both upside (surplus) and downside (deficit) under the plan. Although it is not an express statement of 50/50 sharing, it would presumably inform the expectations of the Sponsors regarding how any surpluses are to be utilized.

(c) Partners’ Agreement and FMP

While the Partners’ Agreement itself does not address the utilization of surplus, the notion that the Sponsors have “agreed to establish a partnership” for the purposes of designing and administering the OTPP and managing the OTPP fund¹² is reinforced throughout the Partners’ Agreement. For example, Section 4 of the Partners’ Agreement provides that “[t]he partnership established by this agreement is intended to govern all aspects of the plan and the fund...” Similarly, Section 8 of the Partners’ Agreement notes that the partners are jointly responsible for “designing the plan structure, setting the benefits of the plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, making changes to the plan, this agreement or other plan documents, deciding whether or not to file a valuation more frequently than required by the *Pension Benefits Act*, appointing the Board, and defining the role of the Board”. The expectations of the Sponsors regarding how surpluses are to be utilized are presumably informed by the commitment noted above for the partnership established “to govern all aspects of the plan and the fund”.

The procedures pursuant to which surplus may be withdrawn or utilized from the OTPP are identified in the FMP (which forms Appendix “A” to the Partners’ Agreement).

We understand that the FMP was first established in March 2003, as a supplement to the Partners’ Agreement, to provide a guidance framework to the Sponsors for decision-making when the OTPP has a funding surplus or shortfall. Prior to the creation of the FMP, the OTPP was considered fully funded (and surplus could be utilized, including through permanent benefit improvements) where assets equalled at least 100% of liabilities. The FMP is intentionally conservative through prioritizing the preservation of assets until a sufficient surplus “cushion” has been built to justify the utilization of surplus for contribution reductions or benefit improvements.

The FMP contemplates five “funding zones”, each defined by a range. These funding zones provide the Sponsors with guidance as to when, based upon the funding level of the plan, it may be appropriate to (amongst other things) increase or decrease benefits, raise or lower contribution rates or conserve assets. The Sponsors always have the discretion, however, to agree to pursue a course of action that is not expressly provided for in the

¹² Partners’ Agreement, section 1.

FMP. As will be discussed below, the ultimate discretion of the Sponsors is reflected throughout various provisions of the FMP.¹³

In the context of plan surpluses, three funding zones are of relevance, each of which is discussed below in greater detail.

(i) Restoration Zone

Article III of the FMP (Funding Zone – Restoration) (the “**Restoration Zone**”) is the “fully funded” zone where assets equal at least the liabilities, determined on the basis set out in the FMP. It is our understanding that the OTPP is currently in the Restoration Zone.

In the Restoration Zone, benefits cannot be improved and contributions cannot be reduced until certain actions are taken to restore past benefit reductions or past contribution increases. In this regard, Section 3.06 of the FMP provides the following:

Section 3.06 *Application of Restoration Basis Excess*: For purposes of clarity, excesses identified pursuant to Section 3.05 shall be applied in the following order, provided that the partners reserve the right to reconsider such application having regard to the contribution rate and benefits then in effect, prevailing economic circumstances and other relevant factors:

(a) *Bring Escalated Adjustments to 50% for Post-2013 Service*: to provide escalated adjustments up to 50% of the CPI adjustment in respect of service accrued after 2013 for the period covered by the valuation, and assumed thereafter at the same rate;

(b) *Bring Escalated Adjustments to 100%*: to provide escalated adjustments up to 100% of the CPI adjustment for the period covered by the valuation, and assumed thereafter at the same rate;

(c) *Restore Escalated Adjustments for Post-2013 Years*: to provide escalated adjustments to increase, to the extent possible, the current accumulated adjustment ratio for each year after 2013, to the current accumulated adjustment ratio for the period from 2010 to 2013, beginning with the first year in which current escalated adjustments were less than 50% of the run-rate escalated adjustments;

(d) *Restore Escalated Adjustments for Post-2009 Years*: to provide escalated adjustments to increase, to the extent possible, the current

¹³ See, for example, the opening words of Section 3.06 of the FMP, which section provides for various uses of surplus: “... provided that the partners reserve the right to reconsider such application having regard to the contribution rate and benefits then in effect, prevailing economic circumstances and other relevant factors”. See also Section 4.05 and 5.05.

accumulated adjustment ratio for each year after 2009 to the run-rate accumulated adjustment ratio, beginning with the first year in which current escalated adjustments were less than run-rate escalated adjustments;

(e) Provide Benefit Increases or Contribution Rate Reductions: to provide the following:

- (i) an increase in benefits, where the present value of current benefits is less than the present value of run-rate benefits,
- (ii) a reduction in contribution rates, where the present value of current contributions exceeds the present value of basic contributions, or
- (iii) a combination of (i) and (ii).

In summary, the Restoration Zone allows for surplus to be utilized to “restore” foregone indexation (Sections 3.06(a)-(d))¹⁴ and then to either increase benefits to the “run-rate benefit” level (i.e., the long-term target level) or to lower contributions to the basic target rate (or a combination of these two options) (Section 3.06(e)). While the FMP contemplates that the actions will typically be taken sequentially (i.e., starting with Section 3.06(a) and ending with the actions in Section 3.06(e)), the Sponsors are required to first agree to the actions taken under Section 3.06 and have the discretion to apply the actions in a different order or to take different action (or to take no action to utilize the surplus).¹⁵

As noted, under Section 3.06(e), surplus can be utilized to reduce contribution rates “where the present value of current contributions exceed the present value of basic contributions” (the “**Restoration Contribution Reduction**”). We understand that in 2001 the Sponsors agreed to a 1.1% increase to both member/employer contributions (phased in over a three year period) to address a funding deficit in the OTPP and that the Restoration Contribution Reduction under Section 3.06(e) would permit these additional contributions to be eliminated, thus restoring contributions to the “basic” level.

The 2013 Term Sheet sets out an agreement between the Sponsors that is in effect from December 31, 2012 to December 30, 2017 (the “**Freeze Period**”), the terms of which are reflected in the FMP. Under Section 3.08 of the FMP, there are certain limits (relating to

¹⁴ This is achieved by first increasing go-forward indexing to 50% for the post-2013 service period, then to 100% on all post-2009 service periods and next, by restoring current pension amounts to a certain prescribed level starting with the years where indexing was less than 50% until all years of partial indexation are restored to the same level and then by restoring indexation to 100% for all service periods.

¹⁵ As noted above, pursuant to Section 3.06 of the FMP, “the partners reserve the right to reconsider such application having regard to the contribution rate and benefits then in effect, prevailing economic circumstances and other relevant factors...”

the funded status of the OTPP) on the ability to make escalated adjustments or to improve benefits pursuant to Section 3.06 during the Freeze Period.

As noted below, no action can be taken under the Temporary Improvement Zone (as defined below) or the Permanent Improvement Zone (as defined below) until all restorative actions under Section 3.06 of the FMP have been provided for (subject to the general discretion of the Sponsors to deviate from the guidelines set out in the FMP).

(ii) Temporary Improvement Zone

Article IV of the FMP (Funding Zone – Temporary Improvements) (the “**Temporary Improvement Zone**”) was added to the FMP in March 2015 and allows for: (i) temporary contribution decreases (a contribution holiday), (ii) surplus distribution, and/or (iii) benefit improvements, provided in each case that the plan’s funding level reaches thresholds set out in the FMP.

We understand that in this zone the plan is considered well-funded and able to afford temporary changes, so long as they do not increase the long-term cost of the OTPP. Surplus cannot be utilized under the Temporary Improvement Zone until the Sponsors have provided for all of the changes specified in Section 3.06 of the Restoration Zone (again, subject to the general discretion of the Sponsors to deviate from the guidelines set out in the FMP).¹⁶

In all cases the Sponsors’ prior agreement is required in order for there to be a temporary contribution decrease, a surplus distribution or a benefit improvement.¹⁷ Where the Sponsors agree to a change that would result in surplus being distributed or utilized for a temporary benefit improvement, the Sponsors are required to enter into a written agreement “governing the manner in which the contributions by the Minister and employers may be adjusted to offset any surplus distribution or temporary improvement of benefits that is reflected in the value of the liabilities.”¹⁸ We understand that this provision is a recognition of the partnership of the Province and the OTF, and requires the Sponsors to enter into an agreement addressing the possible value to be obtained by the Province where there is a decision to provide value to the members (but the provision is not a guarantee that such value will in fact be provided to the Province).

We note that, as a temporary measure, the OTF has “first call” rights on 100% of the surplus disclosed in valuation report with a valuation date after December 30, 2017, up to

¹⁶ FMP, section 4.03

¹⁷ FMP, section 4.05.

¹⁸ FMP, section 4.06

certain amounts as set out in the FMP (the “**OTF Call Right**”).¹⁹ The 2013 Term Sheet indicates that “[t]his is a one-time arrangement intended to compensate Plan members for absorbing 100% (rather than 50%) of funding shortfalls arising in the government initiated Freeze Period.” In other words, this one-time opportunity to benefit from surplus utilization is directly linked to the asymmetrical assumption of risk by OTPP plan participants during the Freeze Period. In light of the Freeze Period and the OTF Call Right, it is our understanding that no actions under the Temporary Improvement Zone will be permitted until the Freeze Period has ended and the OTF Call Right in Article VI of the FMP has been satisfied.²⁰

To summarize, the OTF has a contractual right to the future utilization of surplus, up to the value of the OTF Call Right. OTF cannot utilize any surplus available in the OTPP under this negotiated right until the Freeze Period has ended (on December 30, 2017) and a valuation after such date identifies the existence of surplus available for utilization. In light of this negotiated right, surplus cannot be utilized under the Temporary Improvement Zone or the Permanent Improvement Zone (e.g., to cause a temporary or permanent reduction to contributions) until the OTF Call Right has first been satisfied. Once the OTF Call Right has been satisfied, the *status quo* under the FMP will be restored (i.e., the agreement of the parties will be required for any utilization of surplus). In other words, the OTF Call Right reflects a “one-time” agreement and is expressly “without prejudice or precedent for any future situation”.²¹ It is our understanding that the quantum of the OTF Call Right is not presently expected to be material.

(iii) Permanent Improvement Zone

Where the surplus reaches certain levels as set out in the FMP, Article V of the FMP (Funding Zone – Permanent Improvements) (the “**Permanent Improvement Zone**”) will apply. We understand that in the Permanent Improvement Zone adequate funding security is considered to exist to support permanent changes (either an improvement in benefits or a reduction in contributions).

Under the FMP framework, these changes can be introduced only once the Sponsors have already provided for the changes specified in Section 3.06 (i.e., no further action to restore benefits remains to be taken under the Restoration Zone), subject to the general discretion of the Sponsors to deviate from the guidelines set out in the FMP.²²

¹⁹ FMP, section 6.03.

²⁰ See FMP, subsection 1.05(f) and sections 4.05 and 4.09.

²¹ 2013 Term Sheet, paragraph 11(d).

²² FMP, section 5.03.

The Sponsors are required to mutually agree to any change made in the Permanent Improvement Zone. As in the Temporary Improvement Zone, where the Sponsors have agreed to a change which would result in an improvement to member benefits, the Sponsors would be required to enter into a written agreement “governing the manner in which the contributions by the Minister and employers may be adjusted to offset any change in current benefits that is reflected in the value of the liabilities.”²³

In light of the Freeze Period and the OTF Call Right, it is our understanding that no actions under the Permanent Improvement Zone will be permitted until the Freeze Period has ended and the OTF Call Right in Article VI of the FMP has been satisfied.²⁴

3. History of Surplus Utilization

The history of OTPP surplus utilization from the time the OTPP became a jointly-sponsored pension plan²⁵ to the date that the FMP was established (in March 2003) demonstrates a past practice of the Sponsors equally sharing (in the aggregate) the benefits of surplus utilization:

Valuation Date	Surplus/(Deficit)	OTF	Ontario Government	Surplus Remaining
1990	\$(7.8 billion) unfunded liability	Increased contributions by 1% to 8.9%	Agreed to make a series of special payments to eliminate the unfunded liability and match increased contributions	Special payments considered an asset bringing the plan to a \$0 surplus
1993	\$1.5 billion	\$325 million to offset social contract days	Eliminated special payments for \$1.2 billion saving	\$0
1996	\$0.7 billion	\$0.6 billion for benefit improvements and RCA contributions	N/A	\$0.1 billion
1998	\$6.8 billion	\$2.2 billion for benefit improvements	\$4.6 billion to reduce the value of remaining special payments	\$0

²³ FMP, section 5.05(b).

²⁴ See FMP, sections 5.05 and 5.08.

²⁵ The Partners’ Agreement is dated July 15, 1991.

1999	\$3.5 billion	N/A	\$3.5 billion to reduce the value of remaining special payments	\$0
2001	\$6.8 billion	\$6.2 billion for benefit improvements	N/A	\$0.6 billion
2002	\$1.9 billion	Sponsors agreed not to make any changes to benefits or contributions		\$1.9 billion
Total		\$9.3 Billion	\$9.3 Billion	

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

Although surplus utilization prior to 2003 may not have been 50/50 each time, from 1990 to 2002 the aggregate value obtained by each of the Sponsors was equal. In certain instances where the Province received a disproportionate share of the financial benefits from surplus utilization, a commitment was made to the OTF that they would receive future surplus available for utilization. In 1998, \$6.8 billion in surplus was utilized to cause a \$2.2 billion benefit improvement and to provide the Province with a \$4.6 billion reduction in the value of special payments owed by the Province. As part of this negotiation, the OTF and the Province agreed to allow future surplus to be utilized to eliminate the Province's remaining special payments (which resulted in \$3.5 billion surplus being utilized in 1999 to reduce the value of the Province's remaining special payments) and a commitment was made for the next \$6.2 billion in surplus to be available to OTF for benefit improvements (such surplus being utilized for benefit improvements in 2001).²⁶

As noted above, the FMP was introduced in March 2003 to provide a guidance framework to the Sponsors when the OTPP has a funding surplus or shortfall. It is our understanding that there have been at least 2 material amendments to the FMP framework since its introduction. Below is a summary of the key funding decisions since the introduction of the FMP:

Year	Valuation Status and Key Decisions
2003	\$1.5 billion surplus; no changes to benefits or contribution levels. Funding Management Policy adopted by plan sponsors.
2005	A preliminary \$6.1 billion shortfall was resolved, leaving plan with a \$0.1 billion surplus. Shortfall resolved with special contribution rate increases, totalling 3.1% of base earnings by

²⁶ See Ontario Teachers' Pension Plan, "Key Funding Decisions Since 1990", available at: <https://www.otpp.com/documents/10179/765840/-/d4e2fea5-624d-420f-af15-e2daf9bc2711/Key+Funding+Decisions.pdf>

	2009 for teachers, the Ontario government and other employers. OTF used the \$76 million contingency reserve set aside in 2001 to reduce contribution rate increases for members in 2008.
2008	A preliminary \$12.7 billion shortfall was resolved with the introduction of conditional inflation protection for pension benefits earned after 2009 and an increase in the basic contribution rate for members and the government to 9% from 8%. Employers agree to make special payments equal to any annual pension increases retirees forgo to a maximum of 50% missed inflation.
2009	A preliminary \$2.5 billion shortfall was resolved primarily by assuming a slightly higher long-term rate of return on investments: yield on real-return bonds plus 1.5%, versus real-return bonds plus 1.4%. Other minor changes made to assumptions to reflect recent plan experience.
2011	A preliminary \$17.2 billion shortfall was resolved with a 1.1% contribution rate increase (phased in over three years), slightly smaller annual cost-of-living increases for teachers who retired after 2009, and recognition of current contribution rate as the permanent base rate.
2012	\$9.6 billion preliminary shortfall adjusted to reflect changes in mortality assumptions and impact of two-year freeze on teachers' salaries. 2012 shortfall resolved by making inflation protection for pension credit earned after 2013 fully conditional on plan's funded status and providing slightly smaller pension increases, beginning in 2014, for members who retired after 2009. These changes enabled the plan to assume a slightly higher discount rate. The changes left the plan with a \$200 million surplus at Jan. 1, 2012.
2014	\$5.1 billion preliminary funding surplus used to boost pensions of members who retired after 2009 to the level they would have been at if full inflation protection had been provided each year since they retired. The surplus funds were also used to raise conditional inflation protection to 60% of the increase in the cost of living for the portion of retirees' pensions earned after 2009. Both changes are effective with January 2015 pension payments.
2015	Some of the \$6.8 billion preliminary funding surplus was used to boost pensions of members who retired after 2009 to the level they would have been at if full inflation protection had been provided on January 1, 2015. The surplus funds were also used to raise conditional inflation protection for pension credit earned after 2009 to 70% from 60% of the increase in the cost of living. Both changes were effective January 2016. In addition, some surplus funds were reserved to help facilitate stability in contribution and benefit levels should a future funding valuation show a decline in assets or increase in pension costs.

* Source: Ontario Teachers' Pension Plan, "Key Funding Decisions Since 1990"

In September 2016, the Sponsors announced that a portion of the \$13.2 billion in funding surplus would be utilized to restore inflation increases, with the remaining surplus funds

to be reserved “to help facilitate stability in contribution and benefit levels should a future funding valuation show a decline in assets or increase in pension costs”.²⁷

In summary, surplus has been utilized three times since the FMP was introduced – in each of 2014, 2015 and 2016 escalated adjustments were provided to increase the pensions of members who had retired after 2009. As noted above, the OTPP is currently in the Restoration Zone which, pursuant to Section 3.06, prioritizes the utilization of surplus to “restore” foregone indexation before any other actions are taken with respect to surplus. In other words, since the FMP was established the OTPP has not reached a level of surplus under the FMP which would allow for the Sponsors to enter into an agreement regarding its utilization under the Temporary Improvement Zone or the Permanent Improvement Zone.

It is also notable that, consistent with the 50/50 cost sharing principle under the plan, there is recent precedent for the Sponsors agreeing to equally share in the cost of funding a plan deficit (as with the case of surplus utilization, the Sponsors are required to mutually agree upon how to address any funding deficit in the OTPP). Specifically, the preliminary \$17.2 billion shortfall identified in 2011 was resolved through a 1.1% increase to the contribution rate for both the participating employers and plan members (phased in over a three-year period).

Given the historical use of surplus under joint sponsorship of the OTPP prior to the adoption of the FMP, and the fact that over that time the Sponsors shared equally in surpluses, it may be that the Sponsors will expect to also share future surpluses on an equal basis, at least over time (we understand that it is certainly the Province’s expectation that this will happen). In any event, based on the Plan Documentation, both parties will have an equal opportunity to benefit from surplus utilization through the negotiation process.

V. LEGAL RIGHT OF THE PROVINCE TO UNILATERALLY UTILIZE SURPLUS

As discussed in Part IV of this opinion, the Plan Documentation allows for the Sponsors to agree to utilize surplus in a variety of circumstances, depending on the funded status of the OTPP. These surplus utilization options include the following avenues through which the Province may potentially receive a financial benefit through the utilization of surplus:

²⁷ Ontario Teachers’ Pension Plan, “Funding News”, available at: <https://www.otpp.com/corporate/plan-funding/funding-updates>. We assume that a written agreement was reached by the Sponsors in this regard; however, we have not been provided with a copy of such agreement.

1. In the Restoration Zone, a Restoration Contribution Reduction may be agreed upon, once certain other requisite conditions have been met.
2. In the Temporary Improvement Zone, surplus may be utilized to provide a temporary contribution reduction (a contribution holiday), either as a stand-alone measure or in combination with other surplus utilization options (i.e., benefit improvements or surplus withdrawal).
3. In the Permanent Improvement Zone, surplus may be utilized to permanently reduce the current contribution obligations of the employers and the members, either as a stand-alone measure or in combination with changes to benefits.

Notwithstanding the foregoing, as noted above, the Sponsors have the discretion to, by mutual agreement, utilize surplus in any other manner agreed upon. (For example, Section 5.05 which relates to the Permanent Improvement Zone provides that “the partners may apply all or part of the [surplus] to change current benefits, current contributions, or both”, subject to certain conditions.)

Any enforceable legal right of the Province to utilize surplus pursuant to the Partners’ Agreement (and FMP appended thereto) would be grounded in the law of contract, the Partners’ Agreement and the appended FMP being a contract between the Sponsors. A contract is an agreement “...which gives rise to an obligation that may be enforced in the courts.”²⁸ It is our view that the relevant provisions in the Partners’ Agreement²⁹ that contemplate the ability for the Province to receive a financial benefit through the utilization of surplus do not, by themselves, give rise to a legally enforceable right to unilaterally dictate the use of surplus. Such a legally enforceable right would only arise by agreement between the Sponsors, either through negotiations or mediation, or if an order were issued by a board of arbitration as contemplated by the dispute resolution mechanisms found in the Partners’ Agreement (see Section VI of this Opinion for further discussion of the impact of binding arbitration on the Sponsors’ legal rights).

In this regard, the FMP can be thought of as being similar to an “agreement to agree,” which does not create an enforceable legal interest in relation to the utilization of surplus.³⁰ What the Province does have, however, is a right to negotiate with the OTF the

²⁸ CED – Contracts – I Basis of Contract – 1 – Contract Defined.

²⁹ Article III, Section 3.06; Article IV, Section 4.05; and Article V, Section 5.05.

³⁰ For a statement of the principle that an “agreement to agree” is not an enforceable legal interest, see, for example: *Simpson v. Canada (Attorney General)*, 2011 ONSC 5637 at para. 60 citing *Ward v. Ward*, 2011 ONCA 178 and *Bawitko Investments Ltd. v. Kernels Popcorn Ltd.*, 1991 CanLII 2734 (Ont CA). See also G. H. L. Fridman, *The Law of Contract in Canada*, 6th ed (Toronto: Carswell

use of surplus that may arise under the plan, at least in the context of an actuarial valuation that discloses surplus and that is to be filed with the regulators.

In addition, when a valuation is prepared to be filed and the Sponsors have to discuss the treatment of a surplus disclosed in the valuation, section 74 of the Partners' Agreement requires the Sponsors "to bargain in good faith and make every reasonable effort to reach an agreement on the changes, if any, that will be made to the plan". One might therefore argue that that obligation of good faith may include the obligation to take into account the "sharing" principles described elsewhere in this opinion, given that the OTPP is a jointly-sponsored plan.

As will be discussed below, where the Sponsors are unable to agree upon the utilization of surplus pursuant to the negotiation/mediation processes set forth in the Partners' Agreement, there is an ability for the Sponsors to submit the matter to arbitration. The issuance of an order by an appointed board of arbitration regarding the use of surplus funds under the OTPP would create a legally enforceable right, as the submission to the board of arbitration would constitute a proceeding under the *Arbitrations Act* – as specified in paragraph 87 of the Partners' Agreement – that is enforceable by a court.³¹

VI. IMPACT OF BINDING ARBITRATION ON THE SPONSORS' LEGAL RIGHTS

Section 8.01 of the FMP provides the following:

Section 8.01 Unless the partners mutually agree to the contrary, they shall follow the procedures described in paragraphs 74 to 100 when determining the plan changes arising from Section 3.07.

We first note that the mediation/arbitration process would not be triggered unless there is an actuarial valuation to be filed with the regulators that requires the Sponsors to agree on how any surplus or deficit is to be addressed. If a valuation is prepared in a year when no filing is required (filings generally only being required every three years), and the Sponsors do not agree to file the valuation, then the Sponsors do not necessarily have to address funding and benefit issues and therefore no negotiations may occur.

The processes in paragraphs 74 to 100 of the Partners' Agreement that are referred to in Section 8.01 of the FMP provide, amongst other things, for the following:

Publishing, 2011) at 23 where the author states "There cannot be a contract to enter into a contract. Nor can there be a contract to negotiate, i.e., an agreement to agree."

³¹ Section 50(1) of the *Arbitration Act, 1991*, SO 1991, c 17 states "A person who is entitled to enforcement of an award made in Ontario or elsewhere in Canada may make an application to the court to that effect."

- The Sponsors are required to meet to bargain in good faith and make every reasonable effort to reach an agreement on the changes, if any, that will be made to the plan (section 74);
- The parties may at any point appoint a mediator by agreement of the parties or by a method to which they agree at that time (section 77);
- If the parties agree, the mediator may be appointed as a mediator/arbitrator in which case the appointee will decide on the process and time frame for conducting mediation/arbitration (section 80);
- Within 30 days of appointment, the mediator will prepare a confidential report setting out his or her views on the positions of the two partners and containing a recommendation (section 82);
- If the partners do not accept the report within 14 days of its being delivered to them it will be destroyed and an arbitration board will be appointed (section 84);
- This agreement together with a referral to a board of arbitration constitutes a submission under the *Arbitration Act, 1991*³² (section 87);
- The board of arbitration in making an award will consider prevailing economic conditions and the overall state of the provincial economy (section 91);
- The award made by the board of arbitration, must comply with certain prescribed requirements, including to “provide that the contributions of the Minister and those employers who are required to contribute are equal to the contributions of members” (section 92(c));
- The Board will prepare a final valuation of the plan which implements all of the changes to the plan which have been awarded or agreed to by the partners (section 94);
- The Sponsors may agree to change the procedure described in this agreement, either for one round of negotiations or for all future negotiations; and
- Pursuant to Section 8.02 of the FMP, certain limitations on amendments set out in the FMP also apply to an award made by a board of arbitration (generally, these limitations are intended to ensure that the plan is adequately funded after providing for the utilization of surplus).

³² SO 1991, c. 17 (the “*Arbitration Act*”).

The Partners' Agreement and the FMP contain no general arbitration clause governing all disputes relating to the agreement, although Section 14 of the Partners' Agreement provides for the possibility of voluntary arbitration. We are not aware of any instance where the arbitration provisions have been invoked by the parties since the FMP was established. It is not immediately clear whether disputes relating to the utilization of surplus under Article IV of the FMP (i.e., the Temporary Improvement Zone) and under Article V of the FMP (i.e., the Permanent Improvement Zone) would be subject to arbitration.³³ It is our understanding from discussions with OTPP's internal legal counsel, however, that the arbitration provisions in the FMP would be expected to apply to disputes relating to the utilization of surplus under each of these provisions.

Where a matter has been submitted to arbitration, case law has established that the agreement between the parties that is being arbitrated is the fundamental source of subject matters that come within the arbitration board's jurisdiction.³⁴ The parties are free to design their own procedures, including setting the scope of the arbitration board's jurisdiction and specifying the potential outcomes of the arbitration (subject to certain default appeal rights and mandatory grounds to set aside an award under the *Arbitration Act*). The arbitration board is empowered to make binding decisions because of the arbitration agreement, including any limitations on that authority. Canadian courts have traditionally granted deference to arbitration awards.

Arbitration provisions are generally procedural in nature and therefore do not provide a strong foundation upon which to base parties' reasonable expectations about their substantive rights under an agreement. To resolve a dispute, the arbitration board would engage in an exercise in interpretation of the operative substantive provisions of the relevant governing documents, including any applicable statutory provisions. However, as noted above, under section 92 of the Partners' Agreement, the arbitral award must meet certain mandatory conditions. Among other things, the arbitral award is required to provide that the contributions of the Minister and those employers who are required to contribute are equal to the contributions of members (section 92(c) of the Partners'

³³ On the one hand, Section 8.01 of the FMP provides for the procedures in the Partners' Agreement relating to arbitration to apply "when determining the plan changes arising from Section 3.07". This may suggest that only disputes relating to the utilization of surplus under Article III (i.e., the Restoration Zone) can be arbitrated. On the other hand, Section 8.03 of the FMP provides that "Subject to the 2013 Term Sheet, nothing in Article II to Article IX affects the timing of the triennial negotiation, mediation and arbitration process referred to in paragraph 72 to 100", which may suggest that any agreement relating to the utilization of surplus, including under Article IV or Article V of the FMP, may be subject to arbitration (when a valuation is to be filed the parties have to agree on how any surplus – including surplus in the Temporary Improvement Zone and Permanent Improvement Zone, if any – will be used).

³⁴ See for example: *Desputeaux v. Éditions Chouette* (1987) Inc., [2003] 1 SCR 178, para. 22.

Agreement). The arbitration board does not have discretion to ignore this mandatory provision, although the provision would need to be given effect within the context of the relevant documents and applicable statutes, interpreted as a whole, and other relevant factors, such as past conduct of the parties. As part of the arbitration board's interpretation exercise of the relevant governing documents, in the event of ambiguity in the written terms of the documents, evidence of the parties' post-agreement practices can be admitted as an aid to interpreting the agreement. Past practices may illustrate the parties' intentions at the time of the agreement. These considerations of past practices would be in conjunction with any explicit mandatory considerations set out in the governing document, e.g. prevailing economic conditions and the overall state of the provincial economy under section 91 of the Partners' Agreement. The past practices which the arbitrator may consider would include those described above: the long history of 50/50 member/employer contributions to the plan, and the equal sharing of surpluses prior to 2003 (from 2003 onwards the plan was mostly in deficit, with surpluses used to restore foregone escalated adjustments for members).

Yours truly,

A handwritten signature in dark ink, appearing to read "Osler, Hoskin & Harcourt LLP". The signature is written in a cursive, flowing style.

Osler, Hoskin & Harcourt LLP
JS/DR/JM:jm

RE_OTPP FMP questions.rtf

From: Steele, Jana [JSteele@osler.com]
To: Rienzo, Douglas [DRienzo@osler.com]; Jeff Davis [Jeff_Davis@otpp.com]
CC: Barbara Zvan [Barbara_Zvan@otpp.com]; Marin, Jon [jomarin@osler.com]; Hatzis, Len (TBS) [Len.Hatzis@ontario.ca]; Kaufman, Paul (TBS) [Paul.Kaufman@ontario.ca]
Subject: RE: OTPP FMP questions
Date: Sunday, September 18, 2016 19:10:59

I unfortunately will be on an airplane tomorrow am. Doug, we can catch up later in the day. Thanks Jeff for your help on this question.

Jana

From: Rienzo, Douglas
Sent: Sunday, September 18, 2016 7:09 PM
To: Jeff Davis <Jeff_Davis@otpp.com>
Cc: Barbara Zvan <Barbara_Zvan@otpp.com>; Marin, Jon <jomarin@osler.com>; Hatzis, Len (TBS) <Len.Hatzis@ontario.ca>; Kaufman, Paul (TBS) <Paul.Kaufman@ontario.ca>; Steele, Jana <JSteele@osler.com>
Subject: Re: OTPP FMP questions

Thanks Jeff. I'll try to call you shortly after 9.

If anyone else on this chain wants to participate let me know and I'll circulate a number and time.

Doug

On Sep 18, 2016, at 6:05 PM, Jeff Davis <Jeff_Davis@otpp.com> wrote:

Yes

Jeff Davis

General Counsel, Senior Vice-President,

Corporate Affairs & Corporate Secretary

jeff_davis@otpp.com

Direct [416-730-3753](tel:416-730-3753)

Canadian mobile [416-371-0191](tel:416-371-0191)

US mobile [347-515-4895](tel:347-515-4895)

www.otpp.com

<http://www.otpp.com/documents/10179/729401/red-line.gif/0db64f2b-a6cc-4727-b909-7ee8a8fa-da04?t=1445866411000>

Ontario Teachers' Pension Plan

[5650 Yonge Street, Toronto, Ontario M2M 4H5, Canada](#)

[Ontario Teachers](#)

[FacebookTwitterYoutubeLinkedin](#)

On Sep 18, 2016, at 5:41 PM, Rienzo, Douglas <DRienzo@osler.com> wrote:

Thanks Jeff. Are you around tomorrow morning?

On Sep 18, 2016, at 5:11 PM, Jeff Davis <Jeff_Davis@otpp.com> wrote:

Doug - I think it does apply in those circumstances. I presume you are focused on the phrase "unless the partners otherwise agree...". We shd discuss so I can explain how we read it, in combination with provisions of Art IV and V which refer to the arb provisions. Also, the whole impetus was for an agreement with teeth.

We have in our files a lot of correspondence but that will take time to review.

Let me know when you'd like to chat.

Jeff Davis

General Counsel, Senior Vice-President,

Corporate Affairs & Corporate Secretary

jeff_davis@otpp.com

Direct [416-730-3753](tel:416-730-3753)

Canadian mobile [416-371-0191](tel:416-371-0191)

US mobile [347-515-4895](tel:347-515-4895)

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On Sep 18, 2016, at 2:02 PM, Rienzo, Douglas <DRienzo@osler.com> wrote:

Jeff, we do have one quick question:

As you know there is a mediation/arbitration process contemplated under the Funding Management Policy. It seems to be triggered when decisions have to be made under Article III of the FMP ("Restoration Zone"), but it's not clear that it could apply to any negotiations between the parties regarding surplus utilization under Article IV (temporary improvements) or Article V (Permanent Improvements). Do you know if it was intended for mediation/arbitration to apply to those portions of the FMP?

Also, has there ever been a mediation or arbitration under the FMP?

Doug Rienzo

<image001.gif>

Douglas Rienzo

Partner, Pensions & Benefits

Chair, Diversity Committee

416.862.5683

DIRECT

416.862.6666

FACSIMILE

drienzo@osler.com

Osler, Hoskin & Harcourt LLP
Box 50, 1 First Canadian Place
Toronto, Ontario, Canada M5X 1B8

[<image002.gif>](#)

[<image003.jpg>](#)

From: Jeff Davis [mailto:Jeff_Davis@otpp.com]
Sent: Sunday, September 18, 2016 9:22 AM
To: Steele, Jana <JSteele@osler.com>
Cc: Barbara Zvan <Barbara_Zvan@otpp.com>; Marin, Jon
<jomarin@osler.com>; Rienzo, Douglas <DRienzo@osler.com>; Hatzis,
Len (TBS) <Len.Hatzis@ontario.ca>; Kaufman, Paul (TBS)
<Paul.Kaufman@ontario.ca>
Subject: Re: OTPP FMP questions

Jana -

Let me know you'd like to discuss any of the legal aspects.

Sent from my iPad

On Sep 17, 2016, at 2:25 PM, Steele, Jana <JSteele@osler.com> wrote:

Thanks Barb. And thanks again for your time today. Jana.

Sent from my iPhone

On Sep 17, 2016, at 2:16 PM, Barbara Zvan
<Barbara_Zvan@otpp.com> wrote:

Hi all

Please find attached. BZ

FMP history – this is the document we use for board orientation

FMP Coles Notes – we created this summary in 2015 with a group from the Sponsors and their consulting actuaries and plan actuary

OTPP JSPP agreement – this was the term sheet sent to us. You can see only a small component was added to the FMP. In fact, we spent a lot of time speaking about this, how to incorporate. Given the term nature and low likelihood other benefit reductions would have to be put in place other than CIP, we only insert the small section in 3.08.

Report of Funding – this was a publication in 2002 sent to all plan members, the back page outlines the funds spent in during the “surplus” time of the late 1990s and early 2000s. You can see it was spent evenly so much so that a remaining amount of \$76M (need to 2x check that, but of that order) which is relatively small amount was documented in the Partners’ Agreement to be spent by the OTF at a future date. The \$76M was the amount remaining after round to 0.45% for the CPP offset (vs using something with 6 decimal points). This was “spent” when contributions were later increased via specials, the Teachers had a slightly lower contribution rate for 1st (maybe 2) to offset for this \$76M.

Barbara Zvan, FSA, FCIA, CERA

SVP, Strategy & Risk, Chief Investment Risk Officer

barbara_zvan@otpp.com

Direct 416-730-6364

Assistant: Karen Titus, 416-228-3172, karen_titus@otpp.com

<http://www.otpp.com>

<image001.gif>

Ontario Teachers' Pension Plan

5650 Yonge Street, Toronto, Ontario M2M 4H5, Canada

[<image002.png>](#)

[<image003.png><image004.png><image005.png><image006.png>](#)
=

From: Steele, Jana [<mailto:JSteele@osler.com>]

Sent: Saturday, September 17, 2016 12:01 PM

To: Barbara Zvan <Barbara_Zvan@otpp.com>

Cc: Marin, Jon <jmarin@osler.com>; Rienzo, Douglas

<DRienzo@osler.com>; Hatzis, Len (TBS)

<Len.Hatzis@ontario.ca>; Kaufman, Paul (TBS)

<Paul.Kaufman@ontario.ca>

Subject: Re: OTPP FMP questions

Call in details for 1 pm

416-343-4295

ID: 7801041

Sent from my iPhone

On Sep 17, 2016, at 11:57 AM, Barbara Zvan
<Barbara_Zvan@otpp.com> wrote:

Sure -. Just in the middle of taking my daughter between her activities. Can I call you around 1?

Sent from my BlackBerry 10 smartphone on the Rogers network

From: Steele, Jana

Sent: Saturday, September 17, 2016 11:20 AM

To: Barbara Zvan

Cc: Marin, Jon; Rienzo, Douglas; 'Hatzis, Len (TBS)'; Kaufman, Paul (TBS)

Subject: OTPP FMP questions

Hi Barb:

We were just speaking with Jim Leech regarding the FMP. We are working with the Province of Ontario regarding the accounting issue.

Would you have some time for a call today?

Best regards,

Jana Steele

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<FMP history - updated September 29 by MC new format.pdf>

<FMP Coles Notes.pdf>

<OTPP JSPP Afreement final March 2013.pdf>

<Report on Funding.pdf>

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RE_ URGENT_ Statement of Facts and Assumptions Sept 19.docx.rtf

From: Rienzo, Douglas [DRienzo@osler.com]
To: Hatzis, Len (TBS) [Len.Hatzis@ontario.ca]
CC: Kaufman, Paul (TBS) [Paul.Kaufman@ontario.ca]; Steele, Jana [JSteele@osler.com]; Marin, Jon [jomarin@osler.com]
Subject: RE: URGENT: Statement of Facts and Assumptions Sept 19.docx
Date: Monday, September 19, 2016 15:21:18
Attachment 1: image001.gif
Attachment 2: image002.gif
Attachment 3: image003.jpg

You're welcome, Len.

From: Hatzis, Len (TBS) [mailto:Len.Hatzis@ontario.ca]
Sent: Monday, September 19, 2016 3:11 PM
To: Rienzo, Douglas <DRienzo@osler.com>
Cc: Kaufman, Paul (TBS) <Paul.Kaufman@ontario.ca>; Steele, Jana <JSteele@osler.com>; Marin, Jon <jomarin@osler.com>
Subject: RE: URGENT: Statement of Facts and Assumptions Sept 19.docx

Thanks for turning this around so quickly.

From: Rienzo, Douglas [<mailto:DRienzo@osler.com>]
Sent: September 19, 2016 2:29 PM
To: Hatzis, Len (TBS)
Cc: Kaufman, Paul (TBS); Steele, Jana; Marin, Jon
Subject: RE: URGENT: Statement of Facts and Assumptions Sept 19.docx

Len:

Comments attached.

Doug

Douglas Rienzo

Partner, Pensions & Benefits

Chair, Diversity Committee

416.862.5683

DIRECT

416.862.6666

FACSIMILE

drienzo@osler.com

Osler, Hoskin & Harcourt LLP
Box 50, 1 First Canadian Place
Toronto, Ontario, Canada M5X 1B8

<http://www.osler.com/>

From: Hatzis, Len (TBS) [<mailto:Len.Hatzis@ontario.ca>]

Sent: Monday, September 19, 2016 11:59 AM

To: Steele, Jana <JSteele@osler.com>; Marin, Jon <jomarin@osler.com>; Rienzo, Douglas <DRienzo@osler.com>

Cc: Kaufman, Paul (TBS) <Paul.Kaufman@ontario.ca>

Subject: FW: URGENT: Statement of Facts and Assumptions Sept 19.docx

Importance: High

Jana et al

I know that you have been engaged with Deloitte on these issues, but here are their

draft statement of facts that would be folded into their opinion. We think it would be very useful if you could advise if there are inaccuracies in this – it isn't that long. At first blush, Paul and I made a couple of comments as noted in the attached.

From: Petsche, Nadine (TBS)
Sent: September 19, 2016 11:42 AM
To: Hatzis, Len (TBS); Kaufman, Paul (TBS)
Subject: URGENT: Statement of Facts and Assumptions Sept 19.docx
Importance: High

Len/Paul,

Please advise of any issues. The item has been under review by EDU and ISPPD since 10am, but just checking to see if there are any issues that you see? Please feel free to suggest edits to wording.n

From: Colley, Matthew (CA - Toronto) [<mailto:mcolley@deloitte.ca>]
Sent: September 19, 2016 9:59 AM
To: Petsche, Nadine (TBS); Veinot, Cindy (TBS)
Subject: Statement of Facts and Assumptions Sept 19.docx

Hi – Please find attached the statement of facts and assumptions. There are a couple of comments in this document where we would like OPCD to review the wording before sending onto the AG.

Thanks

Matt

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image001.pdf

OSLER

image002.pdf

osler.com

image003.pdf



RE_ do you have the 2013 term sheet_.rtf

From: Rienzo, Douglas [DRienzo@osler.com]
To: Hatzis, Len (TBS) [Len.Hatzis@ontario.ca]
CC: Steele, Jana [JSteele@osler.com]; Marin, Jon [jomarin@osler.com]
Subject: RE: do you have the 2013 term sheet?
Date: Tuesday, September 20, 2016 14:38:38
Attachment 1: image001.gif
Attachment 2: image002.gif
Attachment 3: image003.jpg
Attachment 4: OTPP JSPP Afreement final March 2013.pdf

Enclosed.

Douglas Rienzo
Partner, Pensions & Benefits

Chair, Diversity Committee

416.862.5683

DIRECT

416.862.6666

FACSIMILE

drienzo@osler.com

Osler, Hoskin & Harcourt LLP
Box 50, 1 First Canadian Place
Toronto, Ontario, Canada M5X 1B8

<http://www.osler.com/>

From: Hatzis, Len (TBS) [mailto:Len.Hatzis@ontario.ca]
Sent: Tuesday, September 20, 2016 2:36 PM
To: Rienzo, Douglas <DRienzo@osler.com>; Marin, Jon <jomarin@osler.com>
Cc: Steele, Jana <JSteele@osler.com>
Subject: FW: do you have the 2013 term sheet?

Can you advise and forward if you have it pls - thanks

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image002.pdf

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image003.pdf



OTPP JSPP Afreement final March 2013.pdf

CONFIDENTIAL

This Term Sheet (the "Agreement") sets out the key terms of the agreement between the Plan Sponsors, which is effective during the "Freeze Period" (as defined below). The Government will provide a letter to the Plan Sponsors which will explain: the background of the 2012 Ontario Budget measures about jointly sponsored pension plans; the Government's plan to introduce legislation to carry out those measures, including pooling of broader public sector pension fund assets; the fact that discussions lead to this Agreement instead; and will confirm the Government Commitments which are based on those discussions and this Agreement.

A. General Principles

1. The Freeze Period runs from December 31, 2012 to December 30, 2017.
2. During the Freeze Period there will be no employer contribution increases except as provided for below. An employer contribution increase is defined as any increase in the employer contribution rate beyond the highest contribution rate provided for in the last valuation filed by the Plan prior to the Freeze Period. Employer contribution increases already scheduled to occur during the Freeze Period as a result of valuations filed with an effective valuation date before December 31, 2012 will occur.
3. During the Freeze Period, except as may be required by the Pension Benefits Act or as a result of a judicial or quasi-judicial decision that is binding upon the Sponsors or the Plan, there will be no benefit improvements unless the Plan's going concern funded status, based on the most recently filed valuation report, on a non-smoothed basis, as of the date that the benefit improvement amendments come into effect meets or exceeds 105%, and the benefit improvement will not bring the going concern funded status below 105% as of the effective date of the amendment.
4. During the Freeze Period, except as may be required by the Pension Benefits Act or as a result of a judicial or quasi-judicial decision that is binding upon the Sponsors or the Plan, there will be no restoration of benefits reduced as a result of application of these principles unless the Plan's going concern funded status, based on the most recently filed valuation report, on a non-smoothed basis, as of the date that the benefit restoration amendments come into effect meets or exceeds 105% and the restoration will not bring the going concern funded status below 105% as of the effective date of the amendment.
5. Ad hoc/conditional indexation is not considered to be a benefit improvement or restoration and Plan amendments to provide or restore ad hoc or conditional cost of living increases to pensioners can be made provided the Plan's going concern funded status on the date that the cost of living increase is agreed upon (based on the most recently prepared valuation report with a valuation date that is no more than twelve months earlier and that uses the same valuation methodology and assumptions that would apply to a filed valuation) exceeds 100% and the cost of living increase will not

bring the going concern funded status below 100% as of the effective date of the amendment.

B. Valuations and Consequential Actions During the Freeze Period

6. Should any draft valuation prepared for filing during the Freeze Period disclose a funding circumstance in which employer contribution increases would normally be implemented (i.e., a funding shortfall) the funding circumstance must be addressed within the following Parameters. Any valuation filed during the Freeze Period will conform to the General Principles above and the Parameters as follows:

a. During the Freeze Period there will be no employer contribution increases except as provided for below. A contribution increase is defined as any increase in the contribution rate beyond the highest contribution rate provided for in the last valuation filed by the Plan prior to the Freeze Period.

b. Any future benefit reductions determined to be required in order to meet the General Principles and these Parameters during the Freeze Period will not exceed twenty percent (20%) of the aggregate value of future benefits determined based on the Plan provisions in effect on December 31, 2011 ("the Benefit Reduction Limit"), which aggregate value the Sponsors agree is \$42.590 billion. Benefit reductions implemented pursuant to the valuation as at January 1, 2012 shall be taken into account for purposes of achieving the 20% Benefit Reduction Limit. For clarity, twenty percent (20%) is measured on an cumulative basis in the Freeze Period.

c. In respect of the benefit reductions provided for under the January 1, 2012 valuation, the Sponsors agree that the reduction in the aggregate value of future benefits is \$4.094 billion (9.6%). This reduction in the aggregate value of future benefits was calculated to include:

(i) the reduction in the funding shortfall from the impact of the decrease in the present value of future benefits and contributions stemming from the increase in the discount rate which resulted from the Plan amendment to remove and replace the remaining 50% guaranteed indexing with full conditional inflation protection ("CIP") for post-2013 service;

(ii) the reduction in present value of benefits from invoking an additional 10% of CIP (inflation protection from 60% to 50%) for post-2009 service effective January 1, 2014 along with the associated increase in the present value of the "share the pain payments" (matching contributions made by the Government/employers) plus the reduction in present value of benefits from invoking a further 5% of CIP (inflation protection from 50% to 45%) for post-2013 service effective January 1, 2015.

Appendix A attached hereto provides further details regarding this benefit reduction calculation.

d. Any future benefit reductions under a post-January 1, 2012 valuation, if necessary, will be implemented with an effective date that is no later than the earlier of:

- i. two years following the valuation date of the filed actuarial valuation, or
- ii. December 30, 2017.

e. In no case will future benefit reductions implemented as a result of the General Principles and/or Parameters affect or reduce pension benefits or ancillary benefits accrued prior to the implementation date of the benefit reduction(s). Ancillary benefits will be considered to have accrued, if, as of the implementation date of the benefit reduction, the person will have met all of the eligibility requirements to exercise the right to receive the ancillary benefits.

f. Sponsors' agreement on future benefit reductions would be effected by a Plan amendment to be prepared and filed within 60 days of agreement or outcome of the dispute resolution process.

g. Once the Benefit Reduction Limit has been reached (i.e., if the second or subsequent valuation(s) filed during the Freeze Period reduce benefits by \$4.424 billion (10.4%)), the Sponsors will return to their usual process and make use of their usual tools (e.g., employer and member contribution rate increases and/or benefit reductions beyond the benefit reduction limit) to determine the steps necessary to avoid:

- i. any remaining shortfall identified in the draft valuation; or
- ii. a future new funding shortfall identified in a subsequent draft valuation during the Freeze Period.

After 2013, any valuation filed during the Freeze Period must be filed on or before September 30 of the year of filing.

C. Dispute Resolution

7. Any dispute with respect to the interpretation or application of this Agreement may be referred by either Sponsor to final and binding arbitration. Either of the parties may notify the other in writing of its desire to submit a difference or dispute to arbitration and the notice shall contain the names of the first party's appointment to an Arbitration Board. The recipient of the notice shall within five (5) days inform the other party of the name of its appointee to the Arbitration Board. The two (2) appointees so selected shall, within five (5) days of the appointment of the second of them, appoint a third person who shall be the Chairperson. If the recipient of a notice fails to appoint an appointee, or the two appointees fail to agree upon a Chairperson within the time limit, either party may request that the appointment shall be made by the Chief Justice for Ontario.

8. In the event that a dispute arises with respect to the interpretation or application of paragraph 6 in particular, all steps to appoint an Arbitration Board as set out in paragraph 7 will be taken on or before 60 days before September 30. The decision of the Arbitration Board shall be issued at least 20 days before September 30.

9. In the event that a dispute arises with respect to the interpretation or application of paragraph 6, in particular, including whether the Benefit Reduction Limit has been reached, the Arbitration Board's mandate will be restricted to determining the means by which the obligations in this Agreement will be carried out and will be subject to the same restrictions applicable to the Sponsors regarding the available options and for greater certainty will exclude an increase in employer contributions during the Freeze Period. The Sponsors, utilizing their usual processes may increase employer contributions once the Benefit Reduction Limit is reached.

D. End of the Freeze Period

10. At the end of the Freeze Period, this Agreement expires and any obligations to conform to this Agreement, and any measures taken in accordance with it, end with the exception of the provisions in paragraph 11.

11. After the end of the Freeze Period, if the Plan's going concern funded status (based on the most recently filed valuation report with a valuation date after December 30, 2017) exceeds 100%, the union/federation sponsors have "first call" on 100% of the surplus disclosed under a valuation report with a valuation date after December 30, 2017, up to a cumulative total of the value of either: the benefit reductions that are made during the Freeze Period; or the Benefit Reduction Limit, whichever is lower. The "first call" on surplus (to take the form of "surplus credits") would be subject to the following conditions:

(a) Surplus credits would only take into account the value of benefit reductions made during the Freeze Period, including the value of benefit reductions made in the January 1, 2012 valuation, but excluding: (i) the value of benefit reductions for which matching contributions are made by the Government/employer ("share the pain payments"), and (ii) the value of benefit reductions relating to the removal and replacement of the remaining 50% guaranteed indexing with full CIP for post-2013 service and the resulting change to the discount rate (as described in paragraph 6(c)(i) above).

(b) Subject to (c) below, the surplus credits could be used as the union/federation sponsors wish (i.e., credits would not be required to be used to restore the same benefits that were reduced during the Freeze Period).

(c) The union/federation sponsors are permitted to spend the surplus credits so long as the going concern funded status of the Plan does not fall below 100% after the surplus credits are spent.

(d) This is a one-time arrangement intended to compensate Plan members for absorbing 100% (rather than 50%) of funding shortfalls arising in the government initiated Freeze Period and is without prejudice or precedent for any future situation.

(e) If inflation protection is invoked below 50% during the Freeze Period, subject to paragraph 11(a), surplus credits will include an amount equal to the actual foregone pension payments during and after the Freeze Period that arise from the reduction in indexing invoked during the Freeze Period until such time as that inflation protection is restored at 50% or more during or after the Freeze Period.

Appendix B attached hereto provides further details regarding the surplus credit calculation.

E. Other Matters

12. The Sponsors will ensure that the cooperation of the Administrator is secured in relation to all aspects of this Agreement, including but not limited to the preparation of the draft valuation, the filed valuation, and applying for any necessary extension of the timelines for filing actuarial valuations and/or Plan amendments as may be necessary to give effect to this Agreement.

13. In order for the terms of this agreement to be effective, the Ontario Government will, subject to Cabinet approval, on or before May 1, 2013, amend Regulation 909 under the Pension Benefits Act to allow for a single four-year valuation cycle for a valuation filing that would otherwise be required to be made during the Freeze Period subject to the following conditions:

- a. at least one valuation is filed during the Freeze Period;
- b. there are no more than four years between the valuation dates of filed valuations; and
- c. any benefit reductions arising from valuations filed during the Freeze Period are implemented in accordance with the General Principles and Parameters herein.

Failing amendment of the said Regulation, this Agreement is of no force or effect.

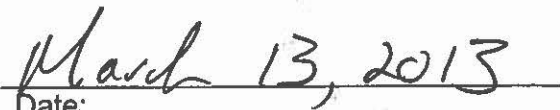
14. The terms of this Agreement supersede all other agreements (written and oral) between the Sponsors, including the Partners' Agreement. The Sponsors shall amend the Plan, the Partners Agreement or any other documents as necessary to give effect to this Agreement.

15. This Agreement may be executed in one or more counterparts and delivered by facsimile or other means of electronic transmission, each of which shall be deemed an original, but all of which taken together shall constitute one and the same agreement.

Liz Sandals - Minister of Education

Date:


Terry Hamilton - President,
Ontario Teachers' Federation


Date:

15. This Agreement may be executed in one or more counterparts and delivered by facsimile or other means of electronic transmission, each of which shall be deemed an original, but all of which taken together shall constitute one and the same agreement.


Liz Sandals - Minister of Education


Date: Mar 14/13

Terry Hamilton – President,
Ontario Teachers' Federation

Date:

Appendix A to Term Sheet Between Government and OTF

As of January 1, 2012 (all amounts in millions)

Calculation of Benefit Reduction Limit

Present Value of Future Benefits Based on Plan Provisions as of December 31, 2011 But Including Legislated Vesting Change	\$ 48,899
Less: Reduction in Present Value of Future Benefits to Reflect Indexation for Post-2009 Service at 60% of CPI	<u>6,309</u>
Equals: Present Value of Future Benefits For Purposes of Calculating Benefit Reduction Limit	\$ 42,590

Benefit Reduction Limit = 20% x \$42,590 = \$8,518

Calculation of Portion of Benefit Reduction Limit Utilized By Changes to Plan Incorporated into January 1, 2012 Actuarial Valuation

Increase in Reduction of Present Value of Future Benefits From Change in Indexation From 60% to 50% of CPI for Post-2009 Service	\$1,367
Plus	
Increase in Government Matching Contributions From Change in Indexation From 60% to 50% of CPI for Post-2009 Service	1,367
Plus	
Reduction in Present Value of Future Benefits Resulting From Change in Discount Rate Associated With Plan Changes (15.0 basis points)	1,390
Plus	
Reduction in Present Value of Future Contributions Resulting From Change in Discount Rate Associated With Plan Changes (15.0 basis points)	(497)
Plus	
Increase in Reduction of Present Value of Future Benefits From Change in Indexation From 50% to 45% of CPI for Post-2013 Service	<u>467</u>
Equals	
Portion of Benefit Reduction Limit Utilized	
\$ Amount	\$ 4,094
% Amount from 20%	9.6%

Remaining Benefit Reduction Limit for Plan Changes in Freeze Period

Benefit Reduction Limit	\$ 8,518
Less: Portion of Benefit Reduction Limit Utilized By Changes to Plan Incorporated into January 1, 2012 Actuarial Valuation	<u>4,094</u>
Equals: Remaining Benefit Reduction Limit For Plan Changes in Freeze Period	\$ 4,424
% Amount from 20%	10.4%

Appendix B to Term Sheet Between Government and OTF

The following are examples only. For purposes of paragraph 11(e) of the Term Sheet, the actual foregone indexing below 50% will be determined by the Plan Administrator based on the actual pension payments affected.

Subject to the above paragraph, the following example shows how the foregone pension payments in respect of which surplus credits are to be awarded (paragraph 11(e)) would be calculated in connection with invoking CIP below 50%. The example is based on:

- Inflation rate of 2.00% per year
- Retirements as of July 1st of each year
- New pensioner payments each year under the additional 50% CIP provisions for post-2013 service of \$3 million times number of years of service from January 1, 2014 to mid-year retirement date
- 10-year period with no mortality reflected
- Indexation at 45% of CPI for the entire period

Calendar Year	Pension Payments With 50% of CPI (000's)	Pension Payments With 45% of CPI (000's)	Foregone Pension Payments (000's)
2014	\$ 1,500	\$ 1,500	\$ 0
2015	\$ 7,515	\$ 7,514	1
2016	\$ 19,592	\$ 19,582	10
2017	\$ 37,786	\$ 37,759	27
2018	\$ 62,164	\$ 62,099	65
2019	\$ 92,786	\$ 92,658	128
2020	\$ 129,714	\$ 129,492	222
2021	\$ 173,011	\$ 172,658	353
2022	\$ 222,741	\$ 222,212	529
2023	\$ 278,968	\$ 278,212	756
			\$ 2,091

The following example modifies the above example to show the impact of moving from 45% of CPI to 0% of CPI (for post-2013 service) effective January 1, 2017:

Calendar Year	Pension Payments With 50% of CPI (000's)	Pension Payments With 45% of CPI / 0% of CPI (000's)	Foregone Pension Payments (000's)
2014	\$ 1,500	\$ 1,500	\$ 0
2015	\$ 7,515	\$ 7,514	1
2016	\$ 19,592	\$ 19,582	10
2017	\$ 37,786	\$ 37,582	204
2018	\$ 62,164	\$ 61,582	582
2019	\$ 92,786	\$ 91,582	1,204
2020	\$ 129,714	\$ 127,582	2,132
2021	\$ 173,011	\$ 169,582	3,429
2022	\$ 222,741	\$ 217,582	5,159
2023	\$ 278,968	\$ 271,582	<u>7,386</u>
			\$ 20,107

RE_ opinion .rtf

From: Kaufman, Paul (TBS) []
To: Hatzis, Len (TBS) [Len.Hatzis@ontario.ca]; Rienzo, Douglas [DRienzo@osler.com]
CC: Marin, Jon [jmarin@osler.com]; Steele, Jana [JSteele@osler.com]
Subject: RE: opinion
Date: Monday, September 19, 2016 22:25:17

Douglas, per Len's email, here are our comments:

Page 2 – para 4 of background – our client has advised that this contains some factual inaccuracies – can this paragraph be corrected to provide as follows: “The Office of the Auditor General has communicated that because the Province does not have the legally enforceable right to unilaterally access the assets of the Plans, and in the absence of that right, because the Province does not have an agreement in place with the joint sponsors as of March 31, 2016 with respect to how the surplus would be utilized such that it would provide a benefit to the Province, the pension assets as presented in the Province's consolidated financial statements should be removed.”

Page 3 – para 1 of conclusions – where it is noted that the Teachers' Act provides for a framework under which an agreement may be entered into – is it possible to note that one has in fact been entered into?

Page 4/5 – para 4 of conclusions – is it possible to emphasize this more prominently in the opinion, i.e. that the applicable legislation and plan documents provide considerations that may shape expectations? – particularly, the point in 4c regarding neither party having a unilateral right meaning that that both parties have an equal opportunity to benefit?

Page 5 – paragraph (a) – third last line – use of the word “typically” – are you using that because you are aware of situations where the split hasn't been 5/50?

Page 12 – is the discussion about the ‘call right’ really relevant to the discussion, given that the quantum is not expected to be material?

Page 16 – last paragraph before section V – can “it may be that” in the fourth last line be made any stronger?

Page 17/18 - Is it necessary that the discussion on page 17/18 be so extensive/definitive, and is the analogy on the top of page 18 really necessary? if the point here is that the FMP does not provide a specific right to utilize the surplus in a particular way (i.e. a unilateral right) that is fair, but is there not room to argue that the FMP is in fact a legally enforceable agreement, especially in light of the intention of the parties as expressed in para 110 of the partners' agreement? Also, consistent with the heading for section V, is it possible to use the term “unilateral” in connection with enforceable legal rights?

Page 20/21 – we are wondering if the last two paragraphs are really necessary to the opinion, and if so, if there is any way that the persuasive value of past practice on any potential arbitration process could be referenced here?

Paul Kaufman
Counsel
Ministry of the Attorney General | Legal Services Branch | Treasury Board Secretariat
9th Floor, 77 Wellesley Street West, Ferguson Block, Toronto, ON M7A 1N3
Phone: 416-327-7012 Fax: 416-325-9404

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-----Original Message-----

From: Hatzis, Len (TBS)
Sent: September-19-16 10:04 PM
To: Rienzo, Douglas
Cc: Marin, Jon; Kaufman, Paul (TBS); Steele, Jana
Subject: Re: opinion

Douglas

No problem - we intend to send some comments by email tonight for your consideration re incorporation into draft. Hopefully these comments make sense in your view and can be accommodated to the extent possible for tomorrow morning. Happy to discuss tomorrow morning

Sent from my BlackBerry 10 smartphone on the Rogers network.

Original Message
From: Rienzo, Douglas
Sent: Monday, September 19, 2016 8:58 PM
To: Hatzis, Len (TBS)
Cc: Marin, Jon; Kaufman, Paul (TBS); Steele, Jana
Subject: Re: opinion

Can we chat in the morning, Len?

> On Sep 19, 2016, at 8:47 PM, Hatzis, Len (TBS) <Len.Hatzis@ontario.ca> wrote:

>

> Can we chat with you later this evening before you look to finalize?

>

> Sent from my BlackBerry 10 smartphone on the Rogers network.

> From: Hatzis, Len (TBS)

> Sent: Monday, September 19, 2016 7:59 PM

> To: Rienzo, Douglas

> Cc: Marin, Jon; Kaufman, Paul (TBS); Steele, Jana

> Subject: Re: opinion

>

>

> Thanks douglas

> I need to review with my clients and will be back to you.

>

> Sent from my BlackBerry 10 smartphone on the Rogers network.

> From: Rienzo, Douglas

> Sent: Monday, September 19, 2016 7:06 PM

> To: Hatzis, Len (TBS)

> Cc: Marin, Jon; Kaufman, Paul (TBS); Steele, Jana

> Subject: RE: opinion

>

>

> Len:

>

> Please find enclosed the draft opinion. Please let us know if you have any comments or questions; subject to your comments we can prepare it in final form. Please note that due to time restrictions we are still reviewing it internally, so there may be some minor changes to be made before finalizing.

>

> Doug
> [cid:image001.gif@01D212A8.CC388EB0]
>
> Douglas Rienzo
> Partner, Pensions & Benefits
> Chair, Diversity Committee
>
>
>
> 416.862.5683
>
> DIRECT
>
> 416.862.6666
>
> FACSIMILE
>
> drienzo@osler.com
>
>
>
>
> Osler, Hoskin & Harcourt LLP
> Box 50, 1 First Canadian Place
> Toronto, Ontario, Canada M5X 1B8
>
> [cid:image002.gif@01D212A8.CC388EB0]<<http://www.osler.com/>>
>
> [2016%20diversity-english]
>
>
>
> From: Hatzis, Len (TBS) [mailto:Len.Hatzis@ontario.ca]
> Sent: Monday, September 19, 2016 3:15 PM
> To: Rienzo, Douglas <DRienzo@osler.com>
> Cc: Marin, Jon <jomarin@osler.com>; Kaufman, Paul (TBS)
> <Paul.Kaufman@ontario.ca>; Steele, Jana <JSteele@osler.com>
> Subject: opinion
>
> Hi
> Any update on delivery of draft opinion . thanks
>
>
>
> Len Hatzis
> Deputy Director
> Legal Services Branch | Treasury Board Secretariat
> 77 Wellesley Street West, 9th Floor, Toronto ON M7A 1N3
> 416.327.6393
>
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> *****

RE_ opinion .rtf

From: Rienzo, Douglas [DRienzo@osler.com]
To: Hatzis, Len (TBS) [Len.Hatzis@ontario.ca]
CC: Marin, Jon [jomarin@osler.com]; Kaufman, Paul (TBS) [Paul.Kaufman@ontario.ca]; Steele, Jana [JSteele@osler.com]
Subject: RE: opinion
Date: Monday, September 19, 2016 19:05:44
Attachment 1: image001.gif
Attachment 2: image002.gif
Attachment 3: image003.jpg
Attachment 4: Draft Osler Opinion re OTTP surplus.pdf

Len:

Please find enclosed the draft opinion. Please let us know if you have any comments or questions; subject to your comments we can prepare it in final form. Please note that due to time restrictions we are still reviewing it internally, so there may be some minor changes to be made before finalizing.

Doug

Douglas Rienzo
Partner, Pensions & Benefits

Chair, Diversity Committee

416.862.5683

DIRECT

416.862.6666

FACSIMILE

drienzo@osler.com

Osler, Hoskin & Harcourt LLP
Box 50, 1 First Canadian Place
Toronto, Ontario, Canada M5X 1B8

<http://www.osler.com/>

From: Hatzis, Len (TBS) [mailto:Len.Hatzis@ontario.ca]
Sent: Monday, September 19, 2016 3:15 PM
To: Rienzo, Douglas <DRienzo@osler.com>
Cc: Marin, Jon <jomarin@osler.com>; Kaufman, Paul (TBS) <Paul.Kaufman@ontario.ca>; Steele, Jana <JSteele@osler.com>
Subject: opinion

Hi

Any update on delivery of draft opinion . thanks

Len Hatzis

Deputy Director

Legal Services Branch | Treasury Board Secretariat

77 Wellesley Street West, 9th Floor, Toronto ON M7A 1N3

416.327.6393

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Draft Osler Opinion re OTPP surplus.pdf

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September 19, 2016

Jana Steele
Direct Dial: 416.862.6625
jsteele@osler.com

Douglas Rienzo
Direct Dial: 416.862.5683
drienzo@osler.com

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PRIVILEGED AND CONFIDENTIAL

Len Hatzis
Deputy Director, Treasury Board Secretariat Legal Services
Ferguson Block
77 Wellesley Street West
9th Floor
Toronto, ON M7A 1N3

Paul Kaufman
Counsel, Treasury Board Secretariat Legal Services
Ferguson Block
77 Wellesley Street West
9th Floor
Toronto, ON M7A 1N3

Dear Sirs:

Accounting Treatment of Surplus in the Ontario Teachers' Pension Plan

I. BACKGROUND

We understand the pertinent background facts to be the following:

1. The Ontario Teachers' Pension Plan (the "**OTPP**") is a jointly-sponsored defined benefit pension plan established under the *Teachers' Pension Act* (Ontario) and is, subject to certain exceptions, required to comply with the *Pension Benefits Act* (Ontario) as well as the *Income Tax Act* (Canada).
2. The sponsors of the OTPP are the Province of Ontario (the "**Province**") and the Ontario Teachers' Federation (the "**OTF**") (collectively, the "**Sponsors**").

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3. We understand that as at March 31, 2016 the Province's Statement of Financial Position (the "**Public Accounts**") includes a pension asset totalling \$10.6 billion (the "**Pension Asset**") related in part to an accounting surplus under the OTPP.¹
4. The Office of the Auditor General of Ontario has expressed concerns with the Province's inclusion of the Pension Asset in the Public Accounts, for reasons including that in its view the Province does not have a legally enforceable right to withdraw the Pension Asset.²

You asked us to consider the processes pursuant to which the Province may utilize surplus assets in the OTPP in accordance with the Plan Documentation (as defined below), and to identify any considerations that might inform the expectations of the Province as a Sponsor regarding the basis upon which decisions will be made relating to surplus utilization. We are not providing an opinion on the proper application of the accounting standards to the present situation, as that is an issue for the accountants to address.

II. SCOPE OF OPINION

For the purposes of our opinion, we considered the following documentation (collectively, the "**Plan Documentation**"):

1. The Ontario Teachers' Pension Plan (the "**OTPP**" or "**plan**");
2. The 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 (the "**Partners' Agreement**");
3. The Funding Management Policy (the "**FMP**"), which forms Appendix "A" to the Partners' Agreement; and
4. The Term Sheet agreed to by the Sponsors dated March 13, 2013 (the "**2013 Term Sheet**") describing the implications of the Freeze Period (as defined below) on the FMP.

We have also considered the following legislation/regulations:

¹ See letter from Bonnie Lysyk (Auditor General) to Greg Orensak (Deputy Minister, Treasury Board) and Scott Thompson (Deputy Minister, Ministry of Finance), dated September 13, 2016. Part of the surplus relates to another pension plan; we understand that \$10.1 billion relates to the OTPP.

² *Ibid.*

1. The *Teachers' Pension Act* (Ontario) (the “**Teachers’ Act**”); and
2. The *Pension Benefits Act* (Ontario) (the “**PBA**”) and the regulations thereunder (the “**PBR**”).

As per your instructions, we have not evaluated the ability of the Province to benefit from the *withdrawal* of surplus assets from the OTPP (although certain provisions of the FMP cited herein relate to both the withdrawal and other utilization of surplus). Rather, this opinion identifies the processes pursuant to which the Province may receive a financial benefit through the *utilization* of OTPP surplus (e.g., as a result of either a temporary reduction in the Province’s contribution obligations (a contribution holiday) or through changes to the contribution formula that reduce the Province’s contribution obligations).

We note that the concept of an *accounting* surplus is distinct from surplus identified in a funding valuation prepared in respect of the OTPP (a “**Funding Valuation**”). Where surplus has been identified in a Funding Valuation, the Plan Documentation provides the Sponsors with certain avenues pursuant to which the Funding Valuation surplus can be utilized. Any reference to “surplus” in this opinion, unless expressly stated otherwise, relates to the surplus identified by the actuary for the OTPP in a Funding Valuation and not to the accounting surplus identified in the Public Accounts. We understand that pursuant to the applicable accounting standards, the recognition of part or all of the accounting surplus on the Public Accounts depends on the ability of the Province to benefit from any surplus in the pension fund over the life of plan.

This opinion does not purport to draw any conclusions, express or implied, about the application of the accounting standards to the present circumstances; rather, it is solely intended to provide the Province with information concerning the legal framework governing the utilization of surplus under the OTPP so as to allow the Province’s accountants to determine whether a related Pension Asset should appear on the Public Accounts.

III. SUMMARY OF OUR CONCLUSIONS

A brief summary of our material conclusions is set forth below (all capitalized terms are defined herein):

1. Paragraph 10(1)3 of the Teachers’ Act provides that the Minister of Education and the executive of the OTF may enter into an agreement (i.e., the Partners’ Agreement) that provides for certain matters, including: “3. The sharing of entitlement to gains or surplus under the plan and of liability for deficiencies in the pension fund by the Minister, the employers who contribute under the plan and the active plan members”. This is a fundamental legislative pronouncement that the Province and the members of the plan are meant to “share” both upside

(surplus) and downside (deficit) under the plan. Although it is not an express statement of 50/50 sharing, it would presumably inform the expectations of the Sponsors regarding how any surpluses are to be utilized.

2. The Plan Documentation (specifically the FMP) and applicable legislation allow for the Sponsors to utilize surplus in a variety of ways, depending on the funded status of the OTPP. These surplus utilization options include the following avenues through which the Province may receive a financial benefit through the utilization of surplus (the three “zones” describe different levels of surplus, a greater amount of surplus being required in order for the next “zone” to come into play):
 - a. In the Restoration Zone, a Restoration Contribution Reduction may be approved once certain other requisite conditions have been met.
 - b. In the Temporary Improvement Zone, surplus may be utilized to provide a temporary contribution reduction (i.e., a contribution holiday), either as a stand-alone measure or in combination with other surplus utilization options (i.e., benefit improvements or surplus withdrawal).
 - c. In the Permanent Improvement Zone, surplus may be utilized to permanently reduce the current contribution obligations of the employers and the members, either as a stand-alone measure or in combination with changes to benefits.

Notwithstanding the foregoing, under the FMP the Sponsors have the discretion to, by mutual agreement, utilize surplus in any other manner.

3. Any enforceable legal right to obtain some value from any surplus pursuant to the Partners’ Agreement (and FMP appended thereto) would be grounded in the law of contract. As the relevant provisions of the FMP require the Sponsors to agree upon the manner in which surplus is to be utilized, neither Sponsor has a legally enforceable right to unilaterally utilize surplus in the OTPP. As such, the provisions in the FMP that contemplate the ability for the Province to receive a financial benefit through the utilization of surplus would not, in and of themselves, give rise to a legally enforceable right.
4. Notwithstanding the foregoing, the Plan Documentation and applicable legislation give rise to the following considerations which may shape the Sponsors’ expectation as to the basis upon which surplus will be utilized (and potentially lead to an expectation of equal sharing of the benefit of any surplus, at least over time):

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- a. The Teachers' Act prohibits the total amount of the contributions payable by the Province (and other participating employers) to exceed the amount of contributions paid by or on behalf of active members in respect of credited service for the year (subject to certain exceptions for payment of a solvency deficiency and where there are insufficient cash and liquid assets in the fund).³ In practice, this has typically resulted in 50/50 sharing of the regular contribution costs between the participating employers (including the Province) and plan members.
- b. The history of surplus utilization after the OTPP became a jointly-sponsored plan and prior to the date that the FMP was established demonstrates a past practice of the Sponsors equally sharing (in the aggregate) the financial benefits of surplus utilization, although surplus was not shared equally each time. Since the time the FMP was established, the OTPP has not reached the requisite level of surplus such that the Sponsors could negotiate its utilization under the Temporary Improvement Zone or Permanent Improvement Zone.
- c. The inability for either party to unilaterally require surplus to be utilized in a particular manner (subject to the OTF Call Right), and the requirement to negotiate and agree (or in the absence of agreement, arbitrate) presents the Sponsors with an equal opportunity to benefit from surplus utilization.
- d. One could argue that the obligation to bargain in "good faith" found in the Partners' Agreement may include the obligation to take into account the "sharing" principles described elsewhere in this opinion, given that the OTPP is a jointly-sponsored plan.
5. In the event that the Sponsors cannot agree upon how surplus is to be utilized in the Restoration Zone, the Temporary Improvement Zone or the Permanent Improvement Zone, the matter can be submitted to an arbitration board of three arbitrators. Arbitration provisions are generally procedural in nature and therefore do not provide a strong foundation upon which to base parties' reasonable expectations about their substantive rights under an agreement. To resolve a dispute, the arbitration board would engage in an exercise in interpretation of the operative substantive provisions of the relevant governing documents, including any applicable statutory provisions. However, the arbitral award must meet certain mandatory conditions set forth in the Partners' Agreement. Among other things, the arbitral award is required to ensure that the contributions of the Minister and those employers who are required to contribute

³ Teachers' Act, subsections 5(1.1), (3) and (7).

are equal to the contributions of members (section 92(c) of the Partners' Agreement).

IV. FRAMEWORK IN THE PLAN DOCUMENTATION FOR SURPLUS UTILIZATION BY THE SPONSORS

1. Joint Sponsorship Plan Design and Cost Sharing

The OTPP qualifies as a “jointly sponsored pension plan” (“**JSPP**”) under the PBA, which has three material implications relevant to the present analysis:

1. Plan Governance – Under a JSPP, the employers (or any persons or entities who make contributions on behalf of the employers or represent the employers) and the members of the pension plan (or any representatives of the members) are jointly responsible for making all decisions about the terms and conditions of the pension plan and any amendments to the pension plan.⁴
2. Funding – The OTPP (and certain other prescribed JSPPs) are exempt from solvency funding requirements under the PBR.⁵
3. Cost Sharing – In a defined benefit pension plan which does not qualify as a JSPP, the employer is solely responsible for funding any going concern unfunded liability or solvency deficiency. Given that the OTPP qualifies as a JSPP, however, the PBA permits members to be required to make contributions in respect of any going concern unfunded liability or solvency deficiency.⁶

With respect to the cost-sharing principle referred to in #3 above, the Teachers' Act contains limitations on the contributions that the Province (and other participating employers) may make under the OTPP:

5(1.1) The total amount of the contributions payable by the Minister of Education and the employers who contribute under the pension plan in respect of any year shall not exceed the amount of contributions payable by or on behalf of active plan members in respect of credited service for that year.

Despite this general principle, under the Teachers' Act the Province is required to make additional contributions to the OTPP fund in the event that there are insufficient assets to

⁴ PBR, subsection 3.1(1).

⁵ PBR, subsection 1.3.1(3).

⁶ See PBA, subsection 1(2) and subsection 55(4).

make required payments out of the fund in any particular year.⁷ The Province is also permitted to make additional contributions in respect of a solvency deficiency⁸ (although, as noted above, solvency funding is not required under the OTPP). Notwithstanding that subsection 5(1.1) of the OTPP provides a *cap* on the Province's normal cost contribution obligation, rather than requiring 50/50 cost sharing, we understand that in practice there has been 50/50 cost sharing of the normal contribution cost under the OTPP during most periods of time since the inception of the plan.⁹ The plan text itself also provides for equal contributions, at the basic level (see sections 25(1) and 26(1)).

Currently, the Sponsors are also required to mutually agree upon how any plan deficits are to be addressed.¹⁰ While not binding upon the Sponsors, the FMP indicates that deficits may be addressed through increases to the contribution rates, lowering the amount of indexation and/or other decreases in benefits.

Joint governance and cost sharing form two of the core features of the OTPP. Consistent with the equal sharing of risk permitted under the JSPP plan design, there is a requirement for decisions relating to plan design and plan amendments to be made jointly by the Sponsors. In this regard, the FMP requires the Sponsors to negotiate and agree upon decisions relating to surplus utilization. Accordingly, the Sponsors can be said to have equal *opportunity* to benefit from surplus utilization through the negotiation process.

2. Provisions in the Legislation and Plan Documentation Relating to the Utilization of Surplus

(a) *Pension Benefits Act*

The PBA and PBR do not mandate any particular treatment of surplus that may arise in a pension plan. One must therefore look to the Teachers' Act, and to the Partners' Agreement and FMP in order to determine how surplus is dealt with under the OTPP.

(b) *Teachers' Pension Act (Ontario)*

Paragraph 10(1)3 of the Teachers' Act provides that the Minister of Education and the executive of the OTF may enter into an agreement (i.e., the Partners' Agreement) that

⁷ Teachers' Act, subsection 5(3).

⁸ Teachers' Act, subsection 5(7).

⁹ See, Ontario Teachers' Pension Plan: "How Contribution Rates Have Evolved" available at: <https://www.otpp.com/documents/10179/20940/-/5e471c2b-23f1-44e6-b5c1-d22e3e50dbc3/How+Contribution+Rates+Have+Evolved.pdf>

¹⁰ See, for example, Section 3.09 and 3.11 of the FMP.

provides for certain matters, including: “3. The sharing of entitlement to gains or surplus under the plan and of liability for deficiencies in the pension fund by the Minister, the employers who contribute under the plan and the active plan members”. This is a fundamental legislative pronouncement that the Province and the members of the plan are meant to “share” both upside (surplus) and downside (deficit) under the plan. Although it is not an express statement of 50/50 sharing, it would presumably inform the expectations of the Sponsors regarding how any surpluses are to be utilized.

(c) Partners’ Agreement and FMP

While the Partners’ Agreement itself does not address the utilization of surplus, the notion that the Sponsors have “agreed to establish a partnership” for the purposes of designing and administering the OTPP and managing the OTPP fund¹¹ is reinforced throughout the Partners’ Agreement. For example, Section 4 of the Partners’ Agreement provides that “[t]he partnership established by this agreement is intended to govern all aspects of the plan and the fund...” Similarly, Section 8 of the Partners’ Agreement notes that the partners are jointly responsible for “designing the plan structure, setting the benefits of the plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, making changes to the plan, this agreement or other plan documents, deciding whether or not to file a valuation more frequently than required by the *Pension Benefits Act*, appointing the Board, and defining the role of the Board”. The expectations of the Sponsors regarding how surpluses are to be utilized are presumably informed by the commitment noted above for the partnership established “to govern all aspects of the plan and the fund”.

The procedures pursuant to which surplus may be withdrawn or utilized from the OTPP are identified in the FMP (which forms Appendix “A” to the Partners’ Agreement).

We understand that the FMP was first established in March 2003, as a supplement to the Partners’ Agreement, to provide a guidance framework to the Sponsors for decision-making when the OTPP has a funding surplus or shortfall. Prior to the creation of the FMP, the OTPP was considered fully funded (and surplus could be utilized, including through permanent benefit improvements) where assets equalled at least 100% of liabilities. The FMP is intentionally conservative through prioritizing the preservation of assets until a sufficient surplus “cushion” has been built to justify the utilization of surplus for contribution reductions or benefit improvements.

The FMP contemplates five “funding zones”, each defined by a range. These funding zones provide the Sponsors with guidance as to when, based upon the funding level of the plan, it may be appropriate to (amongst other things) increase or decrease benefits, raise

¹¹ Partners’ Agreement, section 1.

or lower contribution rates or conserve assets. The Sponsors always have the discretion, however, to agree to pursue a course of action that is not expressly provided for in the FMP. As will be discussed below, the ultimate discretion of the Sponsors is reflected throughout various provisions of the FMP.¹²

In the context of plan surpluses, three funding zones are of relevance, each of which is discussed below in greater detail.

(i) Restoration Zone

Article III of the FMP (Funding Zone – Restoration) (the “**Restoration Zone**”) is the “fully funded” zone where assets equal at least the liabilities, determined on the basis set out in the FMP. It is our understanding that the OTPP is currently in the Restoration Zone.

In the Restoration Zone, benefits cannot be improved and contributions cannot be reduced until certain actions are taken to restore past benefit reductions or past contribution increases. In this regard, Section 3.06 of the FMP provides the following:

Section 3.06 *Application of Restoration Basis Excess*: For purposes of clarity, excesses identified pursuant to Section 3.05 shall be applied in the following order, provided that the partners reserve the right to reconsider such application having regard to the contribution rate and benefits then in effect, prevailing economic circumstances and other relevant factors:

(a) *Bring Escalated Adjustments to 50% for Post-2013 Service*: to provide escalated adjustments up to 50% of the CPI adjustment in respect of service accrued after 2013 for the period covered by the valuation, and assumed thereafter at the same rate;

(b) *Bring Escalated Adjustments to 100%*: to provide escalated adjustments up to 100% of the CPI adjustment for the period covered by the valuation, and assumed thereafter at the same rate;

(c) *Restore Escalated Adjustments for Post-2013 Years*: to provide escalated adjustments to increase, to the extent possible, the current accumulated adjustment ratio for each year after 2013, to the current accumulated adjustment ratio for the period from 2010 to 2013, beginning with the first year in which current escalated adjustments were less than 50% of the run-rate escalated adjustments;

¹² See, for example, the opening words of Section 3.06 of the FMP, which section provides for various uses of surplus: “... provided that the partners reserve the right to reconsider such application having regard to the contribution rate and benefits then in effect, prevailing economic circumstances and other relevant factors”. See also Section 4.05 and 5.05.

(d) Restore Escalated Adjustments for Post-2009 Years: to provide escalated adjustments to increase, to the extent possible, the current accumulated adjustment ratio for each year after 2009 to the run-rate accumulated adjustment ratio, beginning with the first year in which current escalated adjustments were less than run-rate escalated adjustments;

(e) Provide Benefit Increases or Contribution Rate Reductions: to provide the following:

- (i) an increase in benefits, where the present value of current benefits is less than the present value of run-rate benefits,
- (ii) a reduction in contribution rates, where the present value of current contributions exceeds the present value of basic contributions, or
- (iii) a combination of (i) and (ii).

In summary, the Restoration Zone allows for surplus to be utilized to “restore” foregone indexation (Sections 3.06(a)-(d))¹³ and then to either increase benefits to the “run-rate benefit” level (i.e., the long-term target level) or to lower contributions to the basic target rate (or a combination of these two options) (Section 3.06(e)). While the FMP contemplates that the actions will typically be taken sequentially (i.e., starting with Section 3.06(a) and ending with the actions in Section 3.06(e)), the Sponsors are required to first agree to the actions taken under Section 3.06 and have the discretion to apply the actions in a different order or to take different action (or to take no action to utilize the surplus).¹⁴

As noted, under Section 3.06(e), surplus can be utilized to reduce contribution rates “where the present value of current contributions exceed the present value of basic contributions” (the “**Restoration Contribution Reduction**”). We understand that in 2001 the Sponsors agreed to a 1.1% increase to both member/employer contributions (phased in over a three year period) to address a funding deficit in the OTPP and that the Restoration Contribution Reduction under Section 3.06(e) would permit these additional contributions to be eliminated, thus restoring contributions to the “basic” level.

¹³ This is achieved by first increasing go-forward indexing to 50% for the post-2013 service period, then to 100% on all post-2009 service periods and next, by restoring current pension amounts to a certain prescribed level starting with the years where indexing was less than 50% until all years of partial indexation are restored to the same level and then by restoring indexation to 100% for all service periods.

¹⁴ As noted above, pursuant to Section 3.06 of the FMP, “the partners reserve the right to reconsider such application having regard to the contribution rate and benefits then in effect, prevailing economic circumstances and other relevant factors...”

The 2013 Term Sheet sets out an agreement between the Sponsors that is in effect from December 31, 2012 to December 30, 2017 (the “**Freeze Period**”), the terms of which are reflected in the FMP. Under Section 3.08 of the FMP, there are certain limits (relating to the funded status of the OTPP) on the ability to make escalated adjustments or to improve benefits pursuant to Section 3.06 during the Freeze Period.

As noted below, no action can be taken under the Temporary Improvement Zone (as defined below) or the Permanent Improvement Zone (as defined below) until all restorative actions under Section 3.06 of the FMP have been provided for (subject to the general discretion of the Sponsors to deviate from the guidelines set out in the FMP).

(ii) Temporary Improvement Zone

Article IV of the FMP (Funding Zone – Temporary Improvements) (the “**Temporary Improvement Zone**”) was added to the FMP in March 2015 and allows for: (i) temporary contribution decreases (a contribution holiday), (ii) surplus distribution, and/or (iii) benefit improvements, provided in each case that the plan’s funding level reaches thresholds set out in the FMP.

We understand that in this zone the plan is considered well-funded and able to afford temporary changes, so long as they do not increase the long-term cost of the OTPP. Surplus cannot be utilized under the Temporary Improvement Zone until the Sponsors have provided for all of the changes specified in Section 3.06 of the Restoration Zone (again, subject to the general discretion of the Sponsors to deviate from the guidelines set out in the FMP).¹⁵

In all cases the Sponsors’ prior agreement is required in order for there to be a temporary contribution decrease, a surplus distribution or a benefit improvement.¹⁶ Where the Sponsors agree to a change that would result in surplus being distributed or utilized for a temporary benefit improvement, the Sponsors are required to enter into a written agreement “governing the manner in which the contributions by the Minister and employers may be adjusted to offset any surplus distribution or temporary improvement of benefits that is reflected in the value of the liabilities.”¹⁷ We understand that this provision is a recognition of the partnership of the Province and the OTF, and requires the Sponsors to enter into an agreement addressing the possible value to be obtained by the Province where there is a decision to provide value to the members (but the provision is not a guarantee that such value will in fact be provided to the Province).

¹⁵ FMP, section 4.03

¹⁶ FMP, section 4.05.

¹⁷ FMP, section 4.06

We note that, as a temporary measure, the OTF has “first call” rights on 100% of the surplus disclosed in valuation report with a valuation date after December 30, 2017, up to certain amounts as set out in the FMP (the “**OTF Call Right**”).¹⁸ The 2013 Term Sheet indicates that “[t]his is a one-time arrangement intended to compensate Plan members for absorbing 100% (rather than 50%) of funding shortfalls arising in the government initiated Freeze Period and is without prejudice or precedent for any future situation.” In other words, this one-time opportunity to benefit from surplus utilization is directly linked to the asymmetrical assumption of risk by OTTP plan participants during the Freeze Period. In light of the Freeze Period and the OTF Call Right, it is our understanding that no actions under the Temporary Improvement Zone will be permitted until the Freeze Period has ended and the OTF Call Right in Article VI of the FMP has been satisfied.¹⁹ It is our understanding that the quantum of the OTF Call Right is not presently expected to be material.

(iii) Permanent Improvement Zone

Where the surplus reaches certain levels as set out in the FMP, Article V of the FMP (Funding Zone – Permanent Improvements) (the “**Permanent Improvement Zone**”) will apply. We understand that in the Permanent Improvement Zone adequate funding security is considered to exist to support permanent changes (either an improvement in benefits or a reduction in contributions).

Under the FMP framework, these changes can be introduced only once the Sponsors have already provided for the changes specified in Section 3.06 (i.e., no further action to restore benefits remains to be taken under the Restoration Zone), subject to the general discretion of the Sponsors to deviate from the guidelines set out in the FMP.²⁰

The Sponsors are required to mutually agree to any change made in the Permanent Improvement Zone. As in the Temporary Improvement Zone, where the Sponsors have agreed to a change which would result in an improvement to member benefits, the Sponsors would be required to enter into a written agreement “governing the manner in which the contributions by the Minister and employers may be adjusted to offset any change in current benefits that is reflected in the value of the liabilities.”²¹

¹⁸ FMP, section 6.03.

¹⁹ See FMP, sections 4.05 and 4.09.

²⁰ FMP, section 5.03.

²¹ FMP, section 5.05(b).

In light of the Freeze Period and the OTF Call Right, it is our understanding that no actions under the Permanent Improvement Zone will be permitted until the Freeze Period has ended and the OTF Call Right in Article VI of the FMP has been satisfied.²²

3. History of Surplus Utilization

The history of OTPP surplus utilization from the time the OTPP became a jointly-sponsored pension plan²³ to the date that the FMP was established (in March 2003) demonstrates a past practice of the Sponsors equally sharing (in the aggregate) the benefits of surplus utilization:

Valuation Date	Surplus/(Deficit)	OTF	Ontario Government	Surplus Remaining
1990	\$(7.8 billion) unfunded liability	Increased contributions by 1% to 8.9%	Agreed to make a series of special payments to eliminate the unfunded liability and match increased contributions	Special payments considered an asset bringing the plan to a \$0 surplus
1993	\$1.5 billion	\$325 million to offset social contract days	Eliminated special payments for \$1.2 billion saving	\$0
1996	\$0.7 billion	\$0.6 billion for benefit improvements and RCA contributions	N/A	\$0.1 billion
1998	\$6.8 billion	\$2.2 billion for benefit improvements	\$4.6 billion to reduce the value of remaining special payments	\$0
1999	\$3.5 billion	N/A	\$3.5 billion to reduce the value of remaining special payments	\$0
2001	\$6.8 billion	\$6.2 billion for benefit improvements	N/A	\$0.6 billion
2002	\$1.9 billion	Sponsors agreed not to make any changes to benefits or contributions		\$1.9 billion

²² See FMP, sections 5.05 and 5.08.

²³ The Partners' Agreement is dated July 15, 1991.

Total		\$9.3 Billion	\$9.3 Billion	
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* Source: Ontario Teachers' Pension Plan Board "Report on Funding" (April 2002)

Although surplus utilization prior to 2003 may not have been 50/50 each time, from 1990 to 2002 the aggregate value obtained by each of the Sponsors was equal. In certain instances where the Province received a disproportionate share of the financial benefits from surplus utilization, a commitment was made to the OTF that they would receive future surplus available for utilization. In 1998, \$6.8 billion in surplus was utilized to cause a \$2.2 billion benefit improvement and to provide the Province with a \$4.6 billion reduction in the value of special payments owed by the Province. As part of this negotiation, the OTF and the Province agreed to allow future surplus to be utilized to eliminate the Province's remaining special payments (which resulted in \$3.5 billion surplus being utilized in 1999 to reduce the value of the Province's remaining special payments) and a commitment was made for the next \$6.2 billion in surplus to be available to OTF for benefit improvements (such surplus being utilized for benefit improvements in 2001).²⁴

As noted above, the FMP was introduced in March 2003 to provide a guidance framework to the Sponsors when the OTPP has a funding surplus or shortfall. It is our understanding that there have been at least 2 material amendments to the FMP framework since its introduction. Below is a summary of the key funding decisions since the introduction of the FMP:

Year	Valuation Status and Key Decisions
2003	\$1.5 billion surplus; no changes to benefits or contribution levels. Funding Management Policy adopted by plan sponsors.
2005	A preliminary \$6.1 billion shortfall was resolved, leaving plan with a \$0.1 billion surplus. Shortfall resolved with special contribution rate increases, totalling 3.1% of base earnings by 2009 for teachers, the Ontario government and other employers. OTF used the \$76 million contingency reserve set aside in 2001 to reduce contribution rate increases for members in 2008.
2008	A preliminary \$12.7 billion shortfall was resolved with the introduction of conditional inflation protection for pension benefits earned after 2009 and an increase in the basic contribution rate for members and the government to 9% from 8%. Employers agree to make special payments equal to any annual pension increases retirees forgo to a maximum of 50% missed inflation.

²⁴ See Ontario Teachers' Pension Plan, "Key Funding Decisions Since 1990", available at: <https://www.otpp.com/documents/10179/765840/-/d4e2fea5-624d-420f-af15-e2daf9bc2711/Key+Funding+Decisions.pdf>

2009	A preliminary \$2.5 billion shortfall was resolved primarily by assuming a slightly higher long-term rate of return on investments: yield on real-return bonds plus 1.5%, versus real-return bonds plus 1.4%. Other minor changes made to assumptions to reflect recent plan experience.
2011	A preliminary \$17.2 billion shortfall was resolved with a 1.1% contribution rate increase (phased in over three years), slightly smaller annual cost-of-living increases for teachers who retired after 2009, and recognition of current contribution rate as the permanent base rate.
2012	\$9.6 billion preliminary shortfall adjusted to reflect changes in mortality assumptions and impact of two-year freeze on teachers' salaries. 2012 shortfall resolved by making inflation protection for pension credit earned after 2013 fully conditional on plan's funded status and providing slightly smaller pension increases, beginning in 2014, for members who retired after 2009. These changes enabled the plan to assume a slightly higher discount rate. The changes left the plan with a \$200 million surplus at Jan. 1, 2012.
2014	\$5.1 billion preliminary funding surplus used to boost pensions of members who retired after 2009 to the level they would have been at if full inflation protection had been provided each year since they retired. The surplus funds were also used to raise conditional inflation protection to 60% of the increase in the cost of living for the portion of retirees' pensions earned after 2009. Both changes are effective with January 2015 pension payments.
2015	Some of the \$6.8 billion preliminary funding surplus was used to boost pensions of members who retired after 2009 to the level they would have been at if full inflation protection had been provided on January 1, 2015. The surplus funds were also used to raise conditional inflation protection for pension credit earned after 2009 to 70% from 60% of the increase in the cost of living. Both changes were effective January 2016. In addition, some surplus funds were reserved to help facilitate stability in contribution and benefit levels should a future funding valuation show a decline in assets or increase in pension costs.

* Source: Ontario Teachers' Pension Plan, "Key Funding Decisions Since 1990"

In September 2016, the Sponsors announced that a portion of the \$13.2 billion in funding surplus would be utilized to restore inflation increases, with the remaining surplus funds to be reserved "to help facilitate stability in contribution and benefit levels should a future funding valuation show a decline in assets or increase in pension costs".²⁵

²⁵ Ontario Teachers' Pension Plan, "Funding News", available at: <https://www.otpp.com/corporate/plan-funding/funding-updates>. We assume that a written agreement was reached by the Sponsors in this regard; however, we have not been provided with a copy of such agreement.

In summary, surplus has been utilized three times since the FMP was introduced – in each of 2014, 2015 and 2016 escalated adjustments were provided to increase the pensions of members who had retired after 2009. As noted above, the OTPP is currently in the Restoration Zone which, pursuant to Section 3.06, prioritizes the utilization of surplus to “restore” foregone indexation before any other actions are taken with respect to surplus. In other words, since the FMP was established the OTPP has not reached a level of surplus under the FMP which would allow for the Sponsors to enter into an agreement regarding its utilization under the Temporary Improvement Zone or the Permanent Improvement Zone.

It is also notable that, consistent with the 50/50 cost sharing principle under the plan, there is recent precedent for the Sponsors agreeing to equally share in the cost of funding a plan deficit (as with the case of surplus utilization, the Sponsors are required to mutually agree upon how to address any funding deficit in the OTPP). Specifically, the preliminary \$17.2 billion shortfall identified in 2011 was resolved through a 1.1% increase to the contribution rate for both the participating employers and plan members (phased in over a three-year period).

Given the historical use of surplus under joint sponsorship of the OTPP prior to the adoption of the FMP, and the fact that over that time the Sponsors shared equally in surpluses, it may be that the Sponsors will expect to also share future surpluses on an equal basis, at least over time. In any event, based on the Plan Documentation, both parties will have opportunity to benefit from surplus utilization through the negotiation process.

V. LEGAL RIGHT OF THE PROVINCE TO UNILATERALLY UTILIZE SURPLUS

As discussed in Part IV of this opinion, the Plan Documentation allows for the Sponsors to agree to utilize surplus in a variety of circumstances, depending on the funded status of the OTPP. These surplus utilization options include the following avenues through which the Province may potentially receive a financial benefit through the utilization of surplus:

1. In the Restoration Zone, a Restoration Contribution Reduction may be agreed upon, once certain other requisite conditions have been met.
2. In the Temporary Improvement Zone, surplus may be utilized to provide a temporary contribution reduction (a contribution holiday), either as a stand-alone measure or in combination with other surplus utilization options (i.e., benefit improvements or surplus withdrawal).

3. In the Permanent Improvement Zone, surplus may be utilized to permanently reduce the current contribution obligations of the employers and the members, either as a stand-alone measure or in combination with changes to benefits.

Notwithstanding the foregoing, as noted above, the Sponsors have the discretion to, by mutual agreement, utilize surplus in any other manner agreed upon. (For example, Section 5.05 which relates to the Permanent Improvement Zone provides that “the partners may apply all or part of the [surplus] to change current benefits, current contributions, or both”, subject to certain conditions.)

Any enforceable legal right of the Province to utilize surplus pursuant to the Partners’ Agreement (and FMP appended thereto) would be grounded in the law of contract, the Partners’ Agreement and the appended FMP being a contract between the Sponsors. A contract is an agreement “...which gives rise to an obligation that may be enforced in the courts.”²⁶ It is our view that the relevant provisions in the Partners’ Agreement²⁷ that contemplate the ability for the Province to receive a financial benefit through the utilization of surplus do not, by themselves, give rise to a legally enforceable right. Such a legally enforceable right would only arise by agreement between the Sponsors, either through negotiations or mediation, or if an order were issued by a board of arbitration as contemplated by the dispute resolution mechanisms found in the Partners’ Agreement (see Section VI of this Opinion for further discussion of the impact of binding arbitration on the Sponsors’ legal rights).

In this regard, the FMP can be thought of as being similar to an “agreement to agree,” which does not create an enforceable legal interest in relation to the utilization of surplus.²⁸ Because there are a number of different options that are contemplated as to how excess funds could potentially be allocated (e.g. provide for a benefit improvement, provide for a surplus distribution, or modify the contributions), and in light of the fact that the utilization of surplus is subject to the ultimate discretion of the Sponsors, it is unlikely that a court would find the Province to have a legally enforceable right with respect to any particular application of surplus, absent the mutual agreement of the Sponsors to utilize surplus in such manner.

²⁶ CED – Contracts – I Basis of Contract – 1 – Contract Defined.

²⁷ Article III, Section 3.06; Article IV, Section 4.05; and Article V, Section 5.05.

²⁸ For a statement of the principle that an “agreement to “agree” is not an enforceable legal interest, see, for example: *Simpson v. Canada (Attorney General)*, 2011 ONSC 5637 at para. 60 citing *Ward v. Ward*, 2011 ONCA 178 and *Bawitko Investments Ltd. v. Kernels Popcorn Ltd.*, 1991 CanLII 2734 (Ont CA). See also G. H. L. Fridman, *The Law of Contract in Canada*, 6th ed (Toronto: Carswell Publishing, 2011) at 23 where the author states “There cannot be a contract to enter into a contract. Nor can there be a contract to negotiate, i.e., an agreement to agree.” (“*Fridman*”).

To draw another analogy in contract law, the terms of the FMP can be thought of as lacking in “sufficient certainty”²⁹ and cannot be said to be capable of “... the bringing of legal proceedings to compel observance of... the terms of a contract...”³⁰ in relation to an alleged obligation to apply excess funds to a particular purpose.

That being said, when a valuation is prepared to be filed and the Sponsors have to discuss the treatment of a surplus disclosed in the valuation, section 74 of the Partners’ Agreement requires the Sponsors “to bargain in good faith and make every reasonable effort to reach an agreement on the changes, if any, that will be made to the plan”. One might therefore argue that that obligation of good faith may include the obligation to take into account the “sharing” principles described elsewhere in this opinion, given that the OTPP is a jointly-sponsored plan.

As will be discussed below, where the Sponsors are unable to agree upon the utilization of surplus pursuant to the negotiation/mediation processes set forth in the Partners’ Agreement, there is an ability for the Sponsors to submit the matter to arbitration. The issuance of an order by an appointed board of arbitration regarding the use of surplus funds under the OTPP would create a legally enforceable right, as the submission to the board of arbitration would constitute a proceeding under the *Arbitrations Act* – as specified in paragraph 87 of the Partners’ Agreement – that is enforceable by a court.³¹

VI. IMPACT OF BINDING ARBITRATION ON THE SPONSORS’ LEGAL RIGHTS

Section 8.01 of the FMP provides the following:

Section 8.01 Unless the partners mutually agree to the contrary, they shall follow the procedures described in paragraphs 74 to 100 when determining the plan changes arising from Section 3.07.

²⁹ *Fridman*, *supra* note 28 at 20 where the author writes “Uncertainty about some specific obligation may suffice to make impossible the conclusion that there is a contract in effect between the parties.”

³⁰ Daniel Greenberg, ed, *Jowitt’s Dictionary of English Law*, 1st ed (London: Thomson Reuters, 2010) *sub verbo* “Enforce” where it states, “[t]here are two stages – before and after judgment – to both of which the term “enforcement” can be applied. (i) Before judgment, enforcement describes the bringing of legal proceeds to compel observance of, for example, the terms of a contract...”. See also *The Dictionary of Canadian Law*, 3d ed, *sub verbo* “enforceable” citing *U.N.A. v Alberta (Attorney General)*, 192 CarswellAlta 10 at para 55 that enforceable refers to a process “... to enable measures to be taken to secure compliance...”.

³¹ Section 50(1) of the *Arbitration Act*, 1991, SO 1991, c 17 states “A person who is entitled to enforcement of an award made in Ontario or elsewhere in Canada may make an application to the court to that effect.”

We first note that the mediation/arbitration process would not be triggered unless there is an actuarial valuation to be filed with the regulators that requires the Sponsors to agree on how any surplus or deficit is to be addressed. If a valuation is prepared in a year when no filing is required (filings generally only being required every three years), and the Sponsors do not agree to file the valuation, then the Sponsors do not necessarily have to address funding and benefit issues and therefore no negotiations may occur.

The processes in paragraphs 74 to 100 of the Partners' Agreement that are referred to in Section 8.01 of the FMP provide, amongst other things, for the following:

- The Sponsors are required to meet to bargain in good faith and make every reasonable effort to reach an agreement on the changes, if any, that will be made to the plan (section 74);
- The parties may at any point appoint a mediator by agreement of the parties or by a method to which they agree at that time (section 77);
- If the parties agree, the mediator may be appointed as a mediator/arbitrator in which case the appointee will decide on the process and time frame for conducting mediation/arbitration (section 80);
- Within 30 days of appointment, the mediator will prepare a confidential report setting out his or her views on the positions of the two partners and containing a recommendation (section 82);
- If the partners do not accept the report within 14 days of its being delivered to them it will be destroyed and an arbitration board will be appointed (section 84);
- This agreement together with a referral to a board of arbitration constitutes a submission under the *Arbitration Act, 1991*³² (section 87);
- The board of arbitration in making an award will consider prevailing economic conditions and the overall state of the provincial economy (section 91);
- The award made by the board of arbitration, must comply with certain prescribed requirements, including to “provide that the contributions of the Minister and those employers who are required to contribute are equal to the contributions of members” (section 92(c));

³² SO 1991, c. 17 (the “*Arbitration Act*”).

- The Board will prepare a final valuation of the plan which implements all of the changes to the plan which have been awarded or agreed to by the partners (section 94);
- The Sponsors may agree to change the procedure described in this agreement, either for one round of negotiations or for all future negotiations; and
- Pursuant to Section 8.02 of the FMP, certain limitations on amendments set out in the FMP also apply to an award made by a board of arbitration (generally, these limitations are intended to ensure that the plan is adequately funded after providing for the utilization of surplus).

The Partners' Agreement and the FMP contain no general arbitration clause governing all disputes relating to the agreement, although Section 14 of the Partners' Agreement provides for the possibility of voluntary arbitration. We are not aware of any instance where the arbitration provisions have been invoked by the parties since the FMP was established. It is not immediately clear whether disputes relating to the utilization of surplus under Article IV of the FMP (i.e., the Temporary Improvement Zone) and under Article V of the FMP (i.e., the Permanent Improvement Zone) would be subject to arbitration.³³ It is our understanding from discussions with OTPP's internal legal counsel, however, that the arbitration provisions in the FMP would be expected to apply to disputes relating to the utilization of surplus under each of these provisions.

Where a matter has been submitted to arbitration, case law has established that the agreement between the parties that is being arbitrated is the fundamental source of subject matters that come within the arbitration board's jurisdiction.³⁴ The parties are free to design their own procedures, including setting the scope of the arbitration board's jurisdiction and specifying the potential outcomes of the arbitration (subject to certain default appeal rights and mandatory grounds to set aside an award under the *Arbitration Act*). The arbitration board is empowered to make binding decisions because of the

³³ On the one hand, Section 8.01 of the FMP provides for the procedures in the Partners' Agreement relating to arbitration to apply "when determining the plan changes arising from Section 3.07". This may suggest that only disputes relating to the utilization of surplus under Article III (i.e., the Restoration Zone) can be arbitrated. On the other hand, Section 8.03 of the FMP provides that "Subject to the 2013 Term Sheet, nothing in Article II to Article IX affects the timing of the triennial negotiation, mediation and arbitration process referred to in paragraph 72 to 100", which may suggest that any agreement relating to the utilization of surplus, including under Article IV or Article V of the FMP, may be subject to arbitration (when a valuation is to be filed the parties have to agree on how any surplus – including surplus in the Temporary Improvement Zone and Permanent Improvement Zone, if any – will be used).

³⁴ See for example: *Desputeaux v. Éditions Chouette* (1987) Inc., [2003] 1 SCR 178, para. 22.

arbitration agreement, including any limitations on that authority. Canadian courts have traditionally granted deference to arbitration awards.

Arbitration provisions are generally procedural in nature and therefore do not provide a strong foundation upon which to base parties' reasonable expectations about their substantive rights under an agreement. To resolve a dispute, the arbitration board would engage in an exercise in interpretation of the operative substantive provisions of the relevant governing documents, including any applicable statutory provisions. However, as noted above, under section 92 of the Partners' Agreement, the arbitral award must meet certain mandatory conditions. Among other things, the arbitral award is required to provide that the contributions of the Minister and those employers who are required to contribute are equal to the contributions of members (section 92(c) of the Partners' Agreement). The arbitration board does not have discretion to ignore this mandatory provision, although the provision would need to be given effect within the context of the relevant documents and applicable statutes, interpreted as a whole, and other relevant factors, such as past conduct of the parties. In general, however, the prospect of arbitration would not put the Province in any stronger position vis-à-vis its right to obtain value from any plan surplus.

Yours truly,

Osler, Hoskin & Harcourt LLP
JS/DR/JM:jm

Draft

RE_ opinion .rtf

From: Dyczkowski, Marilyn (TBS) []
To: Hatzis, Len (TBS) [Len.Hatzis@ontario.ca]; Steele, Jana [JSteele@osler.com]
CC: Rienzo, Douglas [DRienzo@osler.com]; Marin, Jon [jomarin@osler.com]; Kaufman, Paul (TBS) [Paul.Kaufman@ontario.ca]
Subject: RE: opinion
Date: Tuesday, September 20, 2016 07:52:17

Invite just sent

Marilyn Dyczkowski
EA to the Legal Director
Ministry of the Attorney General | Legal Services Branch | Treasury Board Secretariat
9th Floor, 77 Wellesley Street West, Ferguson Block, Toronto, ON M7A 1N3
Phone: 416-326-8385 Fax: 416-325-9404

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-----Original Message-----

From: Hatzis, Len (TBS)
Sent: September 19, 2016 10:32 PM
To: Steele, Jana
Cc: Rienzo, Douglas; Marin, Jon; Kaufman, Paul (TBS); Dyczkowski, Marilyn (TBS)
Subject: Re: opinion

Thanks - Marilyn will send out conference details in morning .

Sent from my BlackBerry 10 smartphone on the Rogers network.

Original Message
From: Steele, Jana
Sent: Monday, September 19, 2016 10:31 PM
To: Hatzis, Len (TBS)
Cc: Rienzo, Douglas; Marin, Jon; Kaufman, Paul (TBS)
Subject: Re: opinion

Fine for me.

Sent from my iPhone

> On Sep 19, 2016, at 10:21 PM, Hatzis, Len (TBS) <Len.Hatzis@ontario.ca> wrote:
>
> Can we chat at 9 am tomorrow pls
>
> Sent from my BlackBerry 10 smartphone on the Rogers network.
> Original Message
> From: Hatzis, Len (TBS)

> Sent: Monday, September 19, 2016 10:04 PM
> To: Rienzo, Douglas
> Cc: Marin, Jon; Kaufman, Paul (TBS); Steele, Jana
> Subject: Re: opinion
>
>
> Douglas
> No problem - we intend to send some comments by email tonight for your
> consideration re incorporation into draft. Hopefully these comments
> make sense in your view and can be accommodated to the extent
> possible for tomorrow morning. Happy to discuss tomorrow morning
>
> Sent from my BlackBerry 10 smartphone on the Rogers network.
> Original Message
> From: Rienzo, Douglas
> Sent: Monday, September 19, 2016 8:58 PM
> To: Hatzis, Len (TBS)
> Cc: Marin, Jon; Kaufman, Paul (TBS); Steele, Jana
> Subject: Re: opinion
>
>
> Can we chat in the morning, Len?
>
>> On Sep 19, 2016, at 8:47 PM, Hatzis, Len (TBS) <Len.Hatzis@ontario.ca> wrote:
>>
>> Can we chat with you later this evening before you look to finalize?
>>
>> Sent from my BlackBerry 10 smartphone on the Rogers network.
>> From: Hatzis, Len (TBS)
>> Sent: Monday, September 19, 2016 7:59 PM
>> To: Rienzo, Douglas
>> Cc: Marin, Jon; Kaufman, Paul (TBS); Steele, Jana
>> Subject: Re: opinion
>>
>>
>> Thanks douglas
>> I need to review with my clients and will be back to you.
>>
>> Sent from my BlackBerry 10 smartphone on the Rogers network.
>> From: Rienzo, Douglas
>> Sent: Monday, September 19, 2016 7:06 PM
>> To: Hatzis, Len (TBS)
>> Cc: Marin, Jon; Kaufman, Paul (TBS); Steele, Jana
>> Subject: RE: opinion
>>
>>
>> Len:
>>
>> Please find enclosed the draft opinion. Please let us know if you have any comments or questions;
subject to your comments we can prepare it in final form. Please note that due to time restrictions we are
still reviewing it internally, so there may be some minor changes to be made before finalizing.
>>
>> Doug
>> [cid:image001.gif@01D212A8.CC388EB0]
>>
>> Douglas Rienzo

>> Partner, Pensions & Benefits

>> Chair, Diversity Committee

>>

>>

>>

>> 416.862.5683

>>

>> DIRECT

>>

>> 416.862.6666

>>

>> FACSIMILE

>>

>> drienzo@osler.com

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>> Osler, Hoskin & Harcourt LLP

>> Box 50, 1 First Canadian Place

>> Toronto, Ontario, Canada M5X 1B8

>>

>> [cid:image002.gif@01D212A8.CC388EB0]<<http://www.osler.com/>>

>>

>> [2016%20diversity-english]

>>

>>

>>

>> From: Hatzis, Len (TBS) [mailto:Len.Hatzis@ontario.ca]

>> Sent: Monday, September 19, 2016 3:15 PM

>> To: Rienzo, Douglas <DRienzo@osler.com>

>> Cc: Marin, Jon <jomarin@osler.com>; Kaufman, Paul (TBS)

>> <Paul.Kaufman@ontario.ca>; Steele, Jana <JSteele@osler.com>

>> Subject: opinion

>>

>> Hi

>> Any update on delivery of draft opinion . thanks

>>

>>

>>

>> Len Hatzis

>> Deputy Director

>> Legal Services Branch | Treasury Board Secretariat

>> 77 Wellesley Street West, 9th Floor, Toronto ON M7A 1N3

>> 416.327.6393

>>

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>> *****

Re_ OTPP surplus accounting issue - follow-up Q.rtf

From: Steele, Jana [JSteele@osler.com]
To: Allan Shapira [allan.shapira@aonhewitt.com]
CC: Marin, Jon [jomarin@osler.com]; Rienzo, Douglas [DRienzo@osler.com]; Hatzis, Len (TBS) [Len.Hatzis@ontario.ca]
Subject: Re: OTPP surplus accounting issue - follow-up Q
Date: Saturday, September 17, 2016 10:17:52

Thanks Allan.

Sent from my iPhone

On Sep 17, 2016, at 10:15 AM, Allan Shapira <allan.shapira@aonhewitt.com> wrote:

I am around if you need any other information.

Sent from my iPhone

On Sep 17, 2016, at 10:14 AM, Marin, Jon <jomarin@osler.com> wrote:

Allan,
Many thanks for getting back to us so quickly with your comments.

Have a great weekend.

Best regards,
Jon

Sent from my iPhone

On Sep 17, 2016, at 10:09 AM, Allan Shapira <allan.shapira@aonhewitt.com> wrote:

The arbitration issue is a legal issue that I don't think is in my bailiwick.

My reference was to the surplus credits from the term sheet. If there were benefit reductions arising from the application of the term sheet then the members would get a surplus credit from those reductions. I don't think there are any surplus credits so the term sheet provisions are a non-issue.

If the surplus is used contribution reductions for both parties there is an easy symmetry. If the members want to use their surplus for a benefit improvement

then the form of the corresponding value to the government has to be addressed in the side agreement. It is only about the form not whether they get a corresponding value.

Allan

Sent from my iPhone

On Sep 16, 2016, at 1:32 PM, Rienzo, Douglas <DRienzo@osler.com> wrote:

Allan:

We have a few more questions about the technical application of the Funding Management Policy, and are hoping you can help us.

1. You mentioned some restrictions on the use of surplus to benefit members. Aside from the 2013 Term Sheet promises under 6.03 (which you said are not big ticket items, if they end up applying at all), are you referring to the “side agreement” provision in 4.06?

Section 4.06 *Side Agreement*: The commitment value shall be used to provide a surplus distribution referred to in Section 4.04(d) or a temporary benefit improvement referred to in Section 4.04(e) only if the partners have entered into a written agreement governing the manner in which the contributions by the Minister and the Employers may be adjusted to offset any surplus distribution or temporary improvement of benefits that is reflected in the value of the liabilities.

What does that section mean? It refers to an agreement to “offset any surplus distribution or temporary improvement in benefits” – does that mean that the government is supposed to get a contribution reduction of equivalent value if surplus is used for a distribution to members or for a temporary benefit improvement? Are there any other provisions in the FMP like this, that the government can point to as supporting its expectation to benefit from part of the surplus?

2. We understand that every time there is a valuation, the parties must sit down and consider what action to take under Article III, and go to mediation and perhaps to arbitration if they cannot agree (i.e. they follow the procedures set out in sections 74 to 100 of the Partners Agreement). If the plan is in Zone 4 or Zone 5, are the potential actions under Articles IV and V also folded into the mediation/arbitration process? The FMP is unclear on this point, and only seems to refer to that process applying to Article III decisions as set out below:

Section 8.01

Unless the partners mutually agree to the contrary, they shall follow the procedures described in paragraphs 74 to 100 when determining the plan changes arising from Section 3.07.

3. The Partners Agreement contains some guidelines for the arbitrator, in section 92:

92. The award made by the board of arbitration will,

(a) deal only with the contribution rate and/or benefits of the pension plan and otherwise maintain the plan as it is set out in Schedule 1,

(b) comply with the laws of Ontario,

(c) provide that the contributions of the Minister and those employers who are required to contribute are equal to the contributions of members,

(d) be based on the valuation of the plan and the costing of changes to benefits which were prepared by the Board,

(e) ensure that any increase in benefits is adequately funded,

(f) not impair the ability of the Board to fulfil its fiduciary responsibilities,

(g) if it includes benefit improvements, not provide for an increase in

the contribution rate paid by plan members greater than .5% of pensionable salary,

provided that all such awards shall be subject to the limitations referred to in subparagraph EE(2). [emphasis added]

Do you have any idea what the reference to “subparagraph EE(2) means?

Could you perhaps reply by email or, if it's easier, suggest a time when we might chat about this? We have been asked to provide our opinion asap, so if we could speak to you this afternoon that would be ideal. I apologize for the short notice. Thanks, Allan.

Doug

<image001.gif>

Douglas Rienzo

Partner, Pensions & Benefits

Chair, Diversity Committee

416.862.5683

DIRECT

416.862.6666

FACSIMILE

drienzo@osler.com

Osler, Hoskin & Harcourt LLP
Box 50, 1 First Canadian Place
Toronto, Ontario, Canada M5X 1B8

<image002.gif>

<image003.jpg>

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